

## CORPORATE

## SEC's Division of Corporation Finance Issues Guidance on Financial Reporting as a Result of the Ongoing Outbreak of COVID-19



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On March 25, 2020, the SEC's Division of Corporation Finance issued CF Disclosure Guidance Topic No. 9.<sup>11</sup> The guidance reflects the current views of the Division of Corporation Finance, or the Division, in response to the ongoing outbreak of COVID-19. The Division emphasized the rapidly evolving and uncertain nature of the impact of COVID-19 and urged companies to provide timely disclosure that is responsive to the federal securities laws. To that end, the Division highlighted that disclosure of business risks and COVID-19-related effects may be necessary or appropriate in a variety of areas, such as management's discussion and analysis, the business section, risk factors, legal proceedings, disclosure controls and procedures, internal control over financial reporting, and the financial statements.

### Disclosing the Impact of COVID-19

The Division noted that the response to the impact of COVID-19 should be a facts and circumstances determination and companies should tailor their disclosure to the specific circumstances of the company.

To assist companies make responsive disclosures, the Division provided a list of questions to consider. The Division noted that answering many of these questions would require forward-looking statements, but that such statements can be structured to avail companies of the safe harbors in Section 27A of the Securities Act and Section 21E of the Exchange Act. The questions posed by the Division included the following:

- **Financial Condition and Results of Operations:** How has COVID-19 impacted your financial condition and results of operations? In light of changing trends and the overall economic outlook, how do you expect COVID-19 to impact your future operating results and near- and long-term financial condition? Do you expect that COVID-19 will impact future operations differently than how it affected the current period?
- **Capital Resources:** How has COVID-19 impacted your capital and financial resources, including your overall liquidity position and outlook? Has your cost of or access to capital and funding sources, such as revolving credit facilities or other sources, changed, or is it reasonably likely to change? Have your sources or uses of cash otherwise been materially impacted? Is there a material uncertainty about your ongoing ability to meet the covenants of your credit agreements? If a material liquidity deficiency has been identified, what course of action has the company taken or proposed to take to remedy the deficiency? Consider the requirement to disclose known trends and uncertainties as it relates to your ability to service your debt or other financial obligations, access the debt markets, including commercial paper or other short-term financing arrangements, maturity mismatches between borrowing sources and the assets funded by those sources, changes in terms requested by counterparties, changes in the valuation of collateral, and counterparty or customer risk. Do you expect to disclose or incur any material COVID-19-related contingencies?

- **Balance Sheet Issues**: How do you expect COVID-19 to affect assets on your balance sheet and your ability to timely account for those assets? For example, will there be significant changes in judgments in determining the fair value of assets measured in accordance with US GAAP or IFRS?
- **Impairment Analysis**: Do you anticipate any material impairments (e.g., with respect to goodwill, intangible assets, long-lived assets, right-of-use assets, investment securities), increases in allowances for credit losses, restructuring charges, other expenses, or changes in accounting judgments that have had or are reasonably likely to have a material impact on your financial statements?
- **Financial and Operational Issues and Internal Controls**: Have COVID-19-related circumstances such as remote work arrangements adversely affected your ability to maintain operations, including financial reporting systems, internal control over financial reporting, and disclosure controls and procedures? If so, what changes in your controls have occurred during the current period that materially affect or are reasonably likely to materially affect your internal control over financial reporting? What challenges do you anticipate in your ability to maintain these systems and controls?
- **Business Continuity Plans**: Have you experienced challenges in implementing your business continuity plans or do you foresee requiring material expenditures to do so? Do you face any material resource constraints in implementing these plans?
- **Demand Impacts**: Do you expect COVID-19 to materially affect the demand for your products or services?
- **Supply Chain, Distribution and Revenues**: Do you anticipate a material adverse impact of COVID-19 on your supply chain or the methods used to distribute your products or services? Do you expect the anticipated impact of COVID-19 to materially change the relationship between costs and revenues?
- **Human Capital and Labor**: Will your operations be materially impacted by any constraints or other impacts on your human capital resources and productivity?
- **Impact of Travel Restrictions**: Are travel restrictions and border closures expected to have a material impact on your ability to operate and achieve your business goals?

### **Disclosure of Material, Non-Public Information**

The Division reminded companies of their obligation to comply with insider trading regulations during the ongoing disruptions caused by COVID-19. The Division specifically mentioned that if COVID-19 has affected a company in a manner that would be material to investors or where a company has become aware of a risk related to COVID-19 that would be material to investors, the company, its directors and officers, and other corporate insiders who are aware of these material COVID-19 matters should refrain from trading in the company's securities until such information is disclosed to the public.

In addition, the Division further reminded companies of their obligation to comply with Regulation FD. Disclosure of material COVID-19-related matters should not be selectively disseminated, and non-intentional disclosure of material information to a limited group of market participants should be promptly followed by disclosure to the public.

## **Reporting of Earnings and Financial Results**

The Division urged companies to address financial reporting issues earlier than they normally would to account for the potentially complex and uncertain impacts of COVID-19 on their balance sheets and income statements. For example, companies may need to spend more time than usual engaging auditors and experts to determine whether an impairment of goodwill is required or whether reserves for certain line items are appropriate in light of rapidly changing dynamics.

In addition, the Division reminded companies of their obligations under Item 10 of Regulation S-K and Regulation G in reporting non-GAAP financial results. The Division stated that to the extent a company presents a non-GAAP financial measure or performance metric to adjust for or explain the impact of COVID-19, it would be appropriate to highlight why management finds the measure or metric useful and how it helps investors assess the impact of COVID-19 on the company's financial position and results of operations. In the case of earnings releases, the Division would not object to reconciling a non-GAAP measure to a preliminary GAAP result that contains an estimate or range. However, for those filings which require GAAP financial statements, companies should reconcile to GAAP results and not include provisional amounts or a range of estimated results.

The Division further reminded companies that non-GAAP measures should not be chosen solely for the purpose that they make the company's performance appear better. Rather, non-GAAP measures should be disclosed to show investors how a company's management and board of directors are analyzing the current and potential impact of COVID-19 on the company's financial condition and operating results. The Division continued by stating that if a company presents non-GAAP financial measures that are reconciled to provisional amounts or an estimated range of GAAP financial measures, it should explain, to the extent practicable, why the line items or accounting is incomplete, and what additional information or analysis may be needed to complete the accounting.

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*Conscious of the human, operational and financial strain that coronavirus is placing on businesses and organizations worldwide, Jenner & Block has assembled a multi-disciplinary Task Force to support clients as they navigate the legal and strategic challenges of the COVID-19 / Coronavirus situation.*

*For additional information and materials, please visit our COVID-19 / Coronavirus Resource Center.*

**[Click here to visit our COVID-19 / Coronavirus Resource Center](#)**

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[1] Securities And Exchange Commission Division of Corporation Finance, *Coronavirus (COVID-19)* —(March 25, 2020), available at <https://www.sec.gov/corpfin/coronavirus-covid-19>.

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