IMPACTS OF COVID-19
ON PUBLIC COMPANIES

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Introduction

Due to the global scale of the pandemic, nearly every public company experienced some kind of impact, but to varying degrees.

This report looks at what aspects of public company financial reporting and financial health were impacted by COVID-19. Developing a better understanding of what has happened during this unprecedented global event provides valuable insight into the risks facing public companies, auditors, and regulatory agencies that may reoccur with future events.

Quality of Financial Reporting

EXPECTATIONS

The global impact of the pandemic on normal operations posed a risk to the quality of financial reporting.

Disrupted operations subsequently disrupt a company's ability to ensure all required disclosures are accurate, complete, and timely.

The pandemic was likely to have an impact on a company's ability to file required reports in a timely manner and on control environments to reflect the new operating conditions.

REALITY

Late filings were impacted differently based on company location, suggesting impacts related to the timing of the pandemic and the SEC relief.

Disclosed changes in controls primarily related to changes with personnel due to pandemic restrictions, such as lockdowns, and a decreased workforce.

Financial Health

EXPECTATIONS

The volatility and uncertainty of the pandemic destabilized estimates necessary in financial statements, posing a risk to financial health.

Going concerns and impairments are particularly sensitive to underlying estimates.

The pandemic was likely to have an impact on the number of going concern audit opinions and both the number and magnitude of impairments.

REALITY

Overall going concern trends did not shift in 2019, but certain issues cited in going concern opinions did become more prevalent during the pandemic.

The number of impairments increased significantly during the pandemic. Variations in disclosed impairments were noted across company size and industry.

The pandemic has now impacted three separate years, with no signs of fully abating. It is highly likely that certain heightened risks arising from pandemic-related conditions will continue in the years to come, as the world adjusts to a new normal. Some issues had more immediate impacts on public companies during the height of the turmoil, but others may take years to be discovered or disclosed, underscoring the importance of diligence and risk management now and in the future.

Quality of Financial Reporting

Late Filings

KEY INSIGHT

The offered SEC relief that extended deadlines for required reports during the pandemic was taken by nearly 1,000 companies. Small foreign companies and companies in industries with global operations struggled the most with timely filing, but there were not significant widespread delays.

Pandemic-related conditions increased the risk of public companies missing compulsory filing deadlines. Travel restrictions and the need to transition to remote work, coupled with the timing of the pandemic at the conclusion of 2019 into 2020, complicated the normal financial closing process.

To mitigate the anticipated filing delays, the SEC provided conditional regulatory relief for public companies facing pandemic-related challenges. The orders issued by the SEC provided affected companies with additional time to file certain disclosure reports; a 45-day extension was granted in lieu of the standard 15-day and 5-day windows for annual and quarterly reports, respectively.

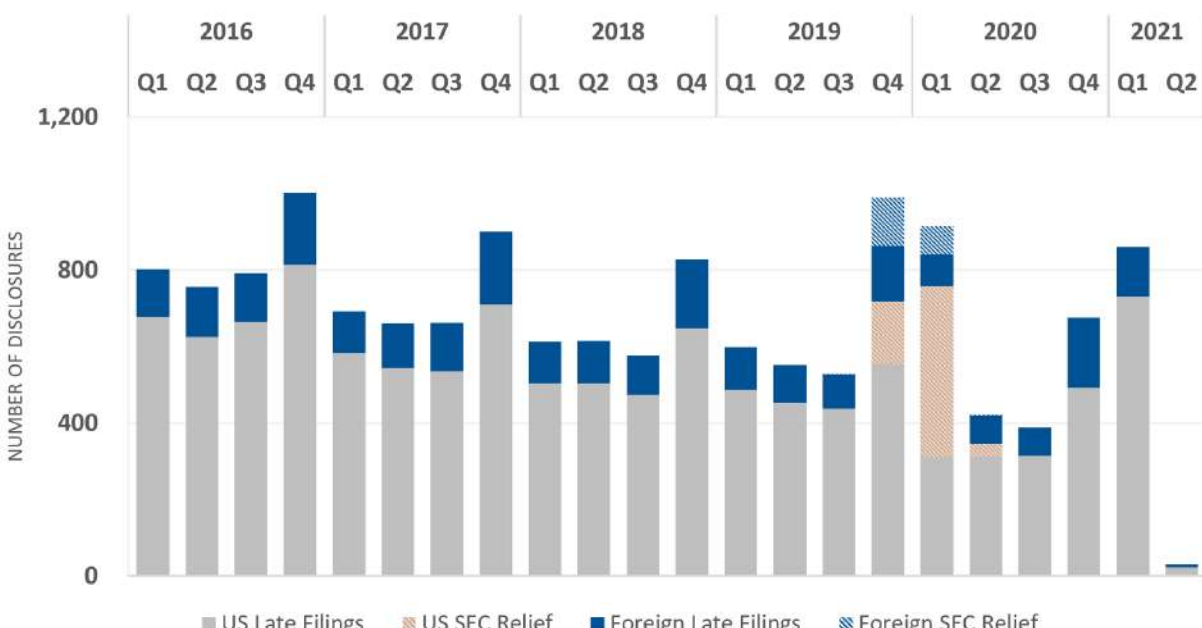
For most companies, the timing of the original SEC order and the extension of the relief applied to disclosures required to be made in the first two quarters of 2020.[1,2]

As anticipated, impacts from COVID-19 contributed to an increased number of late filings for 2019 reports. This reversed a four-year trend of public companies improving their ability to deliver timely information.

Figure 1

Late filing trends and impact of SEC relief during COVID-19

The impact of COVID-19 on timeliness affected foreign-headquartered companies before US companies. Foreign companies had a 51% increase in late filings for Q4 2019 and a 41% increase for Q1 2020. In comparison, US companies had an 11% increase for Q4 2019 and a 56% increase for Q1 2020.



1 SEC Relief Order

2 SEC Relief Extension

Without the SEC relief, the number of late filings for both foreign and US companies in Q1 2020 would be the lowest of any quarter since Q1 2016.

This trend is partially related to the timing of the SEC order. Most companies that took advantage of the SEC relief were small, as the ability to take advantage of the relief was dependent on when the SEC orders were issued in relation to the company's filing deadlines.

Large Accelerated filers that could not file their reports on time did not have the option of SEC relief, as the option was not available until March 1, 2020, after the February 29 filing deadline for large companies. However, in general, large companies are less likely to file late reports than smaller companies due to the amount of resources available to mitigate adverse impacts.

Other than Q1 2020, the remainder of 2020 saw lower numbers of late filings; however, this does not necessarily represent a reversal to pre-pandemic timeliness trends. Q1 2021 saw an increase in the number of late filings and a year-over-year positive change, though this increase was largely unrelated to pandemic impacts.

Figure 2

SEC relief for filing deadlines during COVID-19, by industry

Nearly 60% of all SEC relief in both Q4 2019 and Q1 2020 was taken by companies in two industries: Manufacturing and Services. Manufacturing companies with widespread or global operations were particularly affected by COVID-19 restrictions and supply chain disruptions. Similarly, operations were shuttered at many Services companies due to pandemic lockdowns for non-essential services.

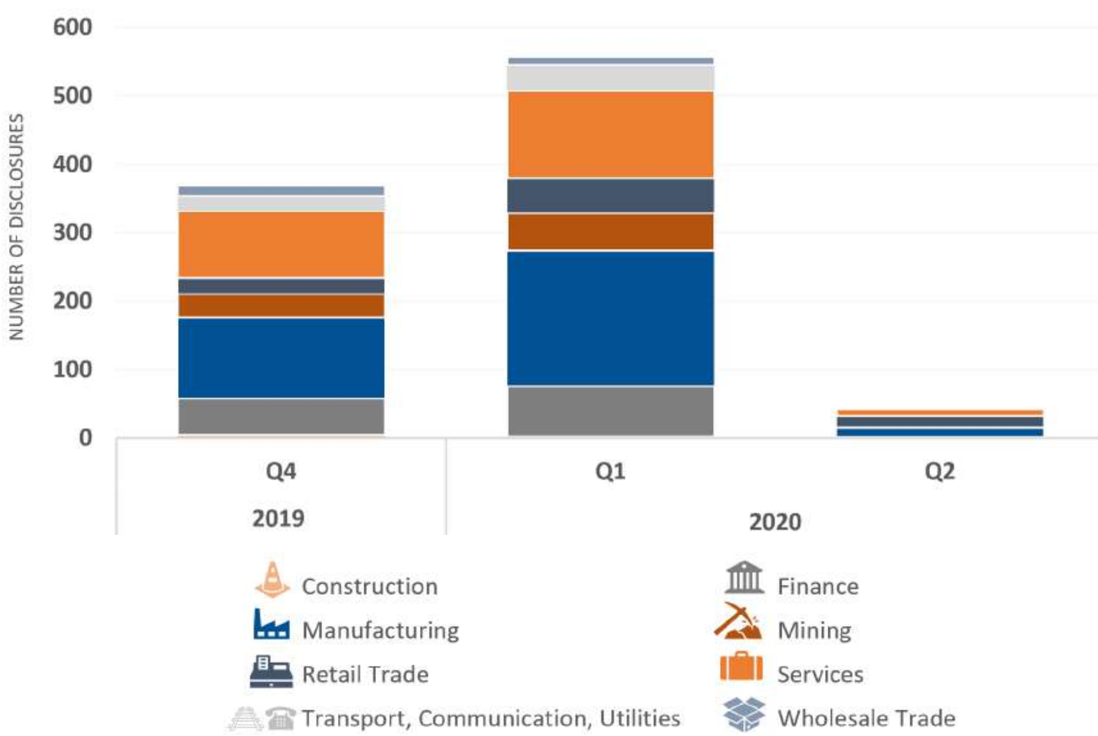


Figure 3

Number of days to issue quarterly reports

(Smaller Reporting Companies and Non-Accelerated Filers)

COVID-19 did not significantly impact the number of days required to file delinquent quarterly reports. The exception is small foreign public companies, which experienced a significant rise in the median number of days to file in Q1 2020.

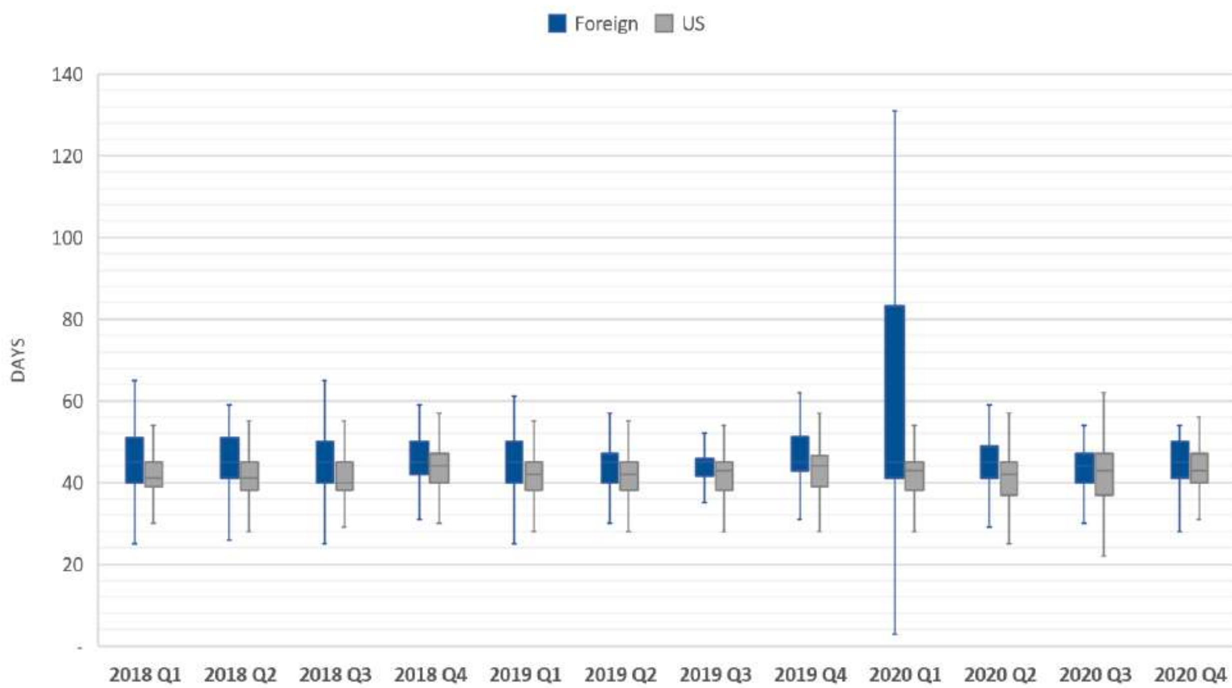
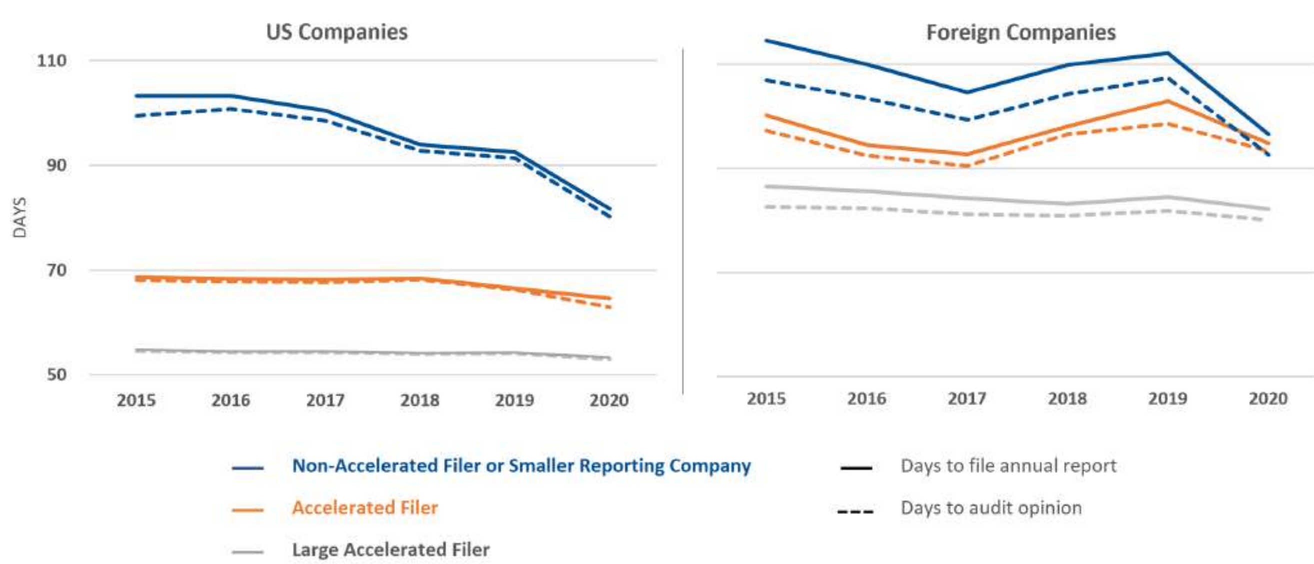


Figure 4

Average number of days to issue annual reports

COVID-19 did not significantly impact the average number of days it took for most public companies to file delinquent annual reports. The exception is foreign Accelerated and Smaller Reporting Companies/Non-Accelerated filers.



Controls

KEY INSIGHT

The rapid changes brought on by the pandemic required changes in controls for many companies related to personnel and remote operating procedures. The disruption of normal processes heightens the risk for material weaknesses in controls, while simultaneously inhibiting remediation efforts.

Companies had to undertake a diverse range of operational adjustments in response to the effects of COVID-19.

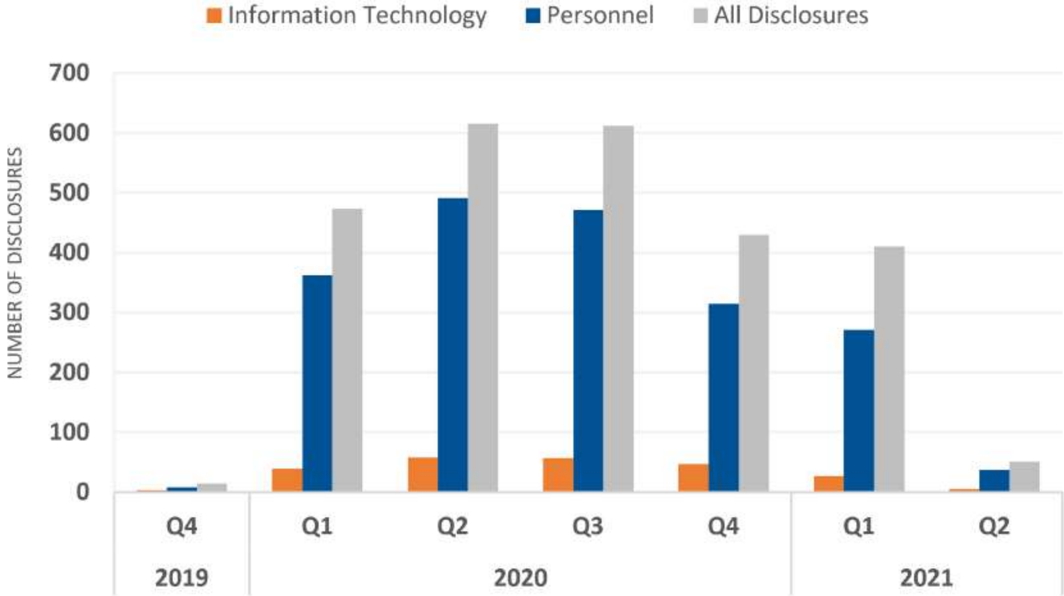
These operational changes heighten the risk of weaknesses and inefficiencies in the control environment, subsequently heightening the risk of a misstatement. As such, any internal or external changes in the environment or operations that can materially impact the internal control structure, business, or financial statements must be monitored and, if necessary, disclosed. This includes the transition to remote work and the accompanying technological developments required to support the shift.

The SEC was acutely aware of the impact the pandemic could have on the control environment. The Office of the Chief Accountant issued a statement in June 2020, emphasizing the importance of disclosing changes that did, or could, materially affect ICFR.[3]

Figure 5

Changes in control environment during COVID-19

Between Q1 2020 and Q1 2021, more than two-thirds of the disclosures related to changes in the control environments at public companies were associated with personnel. Changes related to information technology were a distant second during the pandemic.



3 SEC COVID-19 Disclosure Considerations

Over 800 companies disclosed changes made to their control environment in response to COVID-19.

As expected, based on conditions arising from the pandemic, the most common change related to personnel, distantly followed by changes related to information technology. The majority of the changes in controls were disclosed during Q2 and Q3 2020, reflecting a need for ongoing adjustments in light of the dynamic circumstances.

Aside from changes in controls related to personnel and information technology, certain conditions arising during the pandemic did result in more material impacts on controls. The travel restrictions and a remote workforce impacted the ability to complete physical processes (*see example 1*), in addition to delaying the remediation of weaknesses that were identified (*see example 2*).

Critically, control environments will need to continue to adapt to evolving conditions in order to mitigate the risk of a material weakness that could cause a financial misstatement, error, or other reportable event.

Particularly important for companies going forward are controls related to cybersecurity. As more work is being conducted online and through cloud services, there is an increased risk of cybersecurity breaches, and being able to quickly and effectively mitigate data security issues is an integral component of control systems.

Example 1

Control issues due to COVID-19 impacts will continue to heighten risk of restatement

ONESPAWORLD Holdings Ltd.

"[D]ue to COVID-19 related restrictions, the Company was not able to complete the annual physical counts of inventory on all vessels as is typically done. The Company was able to gain access to certain vessels, and in these instances, we completed counts of individual SKUs. Given the limited access to certain vessels, alternative procedures were performed, including rollforward of inventory from previous counts, analytics by vessels, communication with cruise line partners on the safeguarding and condition of inventory, and overall detailed analysis of inventory condition, consisting of review of excess, slow-moving, expiration of products, and damaged inventories."

Inspired Entertainment, Inc.

"Management has concluded that the misstatements in our footnote disclosures were the result of several unusual events occurring during the fourth quarter 2019 and/or during the related accounting closing and reporting period leading up to our Annual Report on Form 10-K including office closures due to the COVID-19 outbreak, a significant acquisition, first time adoption of accounting standards and which, in the aggregate, contributed to a breakdown in related controls over footnote disclosure review."

Example 2

COVID-19 impacts could delay remediation of control weaknesses

Blink Charging

"During 2020, management has established adequate segregation of duties across all processes except for accounts payable due to pandemic related challenges, and in the area of sales taxes. Management expects to complete the remediation in accounts payable and taxes in the first half of 2021, as the staff return to in-office status."

Financial Health

Going Concerns

KEY INSIGHT

Going concern audit opinions did not increase across companies of all sizes, industries, and locations during the pandemic, despite increased volatility. During the pandemic, new going concerns citing debt covenant concerns and insufficient cash/liquidity became more prominent.

The uncertainty injected by COVID-19 into the current and future economic environment had the potential to significantly impact going concern assessments. Existing uncertainties risked being exposed by the economic instability and shifting macroeconomic trends, as there was no indication of how long the pandemic would last or what the actual impacts would be.

Based on trends in the amount of going concern audit opinions since 2015, COVID-19 had no discernable impact on the overall amount of going concern audit opinions issued for fiscal year 2019.

The amount of going concerns for 2020 may increase as companies continue to file their financial statements for fiscal year 2020. However, based on currently available data, it appears 2020 will have a significant decrease in going concerns.

Figure 6

Going concern trends during COVID-19

Overall, going concern opinions remained stable at 21% in 2017, 2018, and 2019. In 2019, going concern opinions for foreign-headquartered companies decreased from 2018, while US companies experienced no change in the amount of going concerns. This suggests that public companies did not anticipate the impacts from COVID-19 to have adverse long-term effects on financial health.

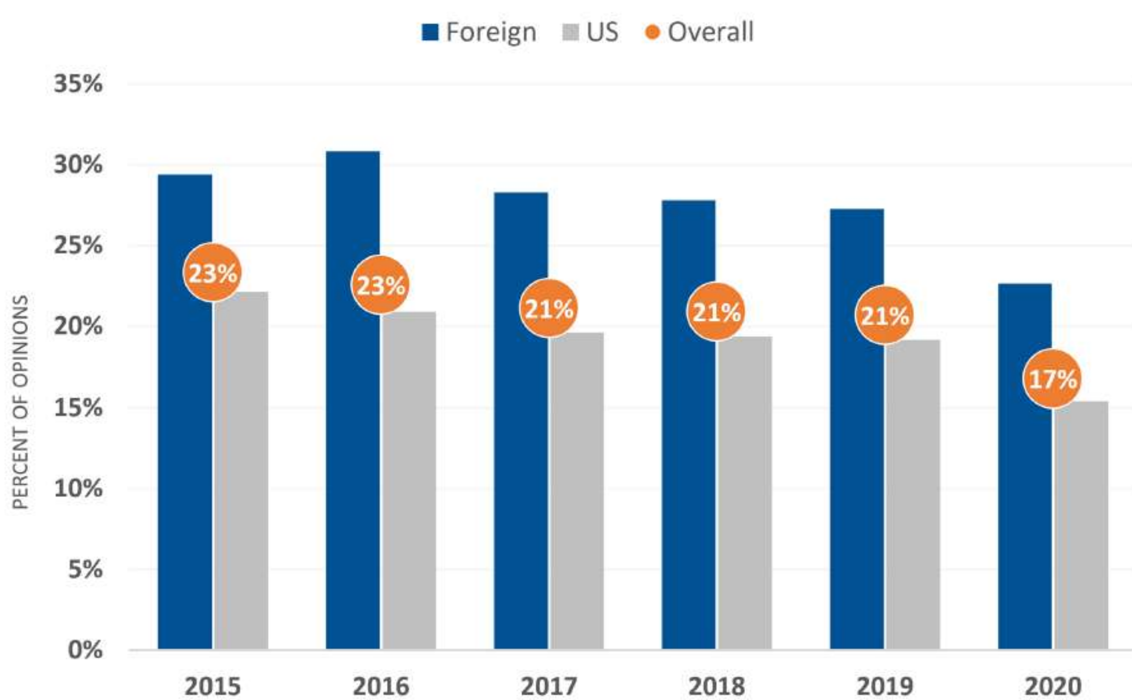


Figure 7

Going concern trends during COVID-19, by company size

In general, going concerns have been decreasing since 2015. Notably, in 2019, Large Accelerated Filers experienced a modest increase in the amount of going concern opinions, while going concerns for Accelerated Filers and Smaller Reporting Companies decreased in 2019.

Figure 8

Year-over-year change in going concern opinions, by industry

Looking at year-over-year changes by industry, 2019 and 2020 saw increases in going concerns in three industries that heavily rely on future estimates to gauge financial health: Construction, Wholesale Trade, and Finance, Insurance and Real Estate. This suggests that, for most industries, any immediate impacts of COVID-19 on financial health were not expected to have long-term substantial impacts that would continue to deteriorate financial position.

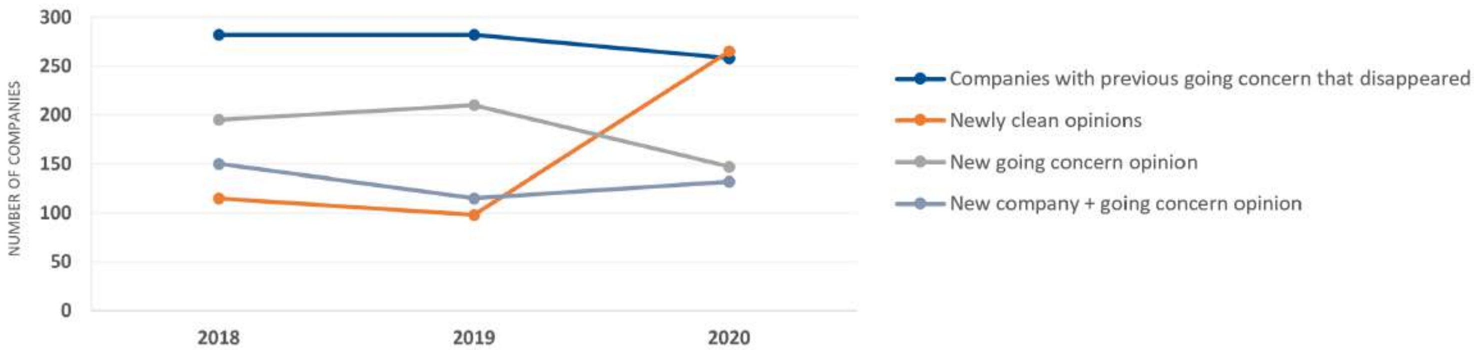
	2016	2017	2018	2019	2020
Agriculture, Forestry, and Fishing	↑	↓	↓	↑	↑
Construction	↑	↑	↑	↓	↗
Finance, Insurance, and Real Estate	↑	↑	↑	↑	↓
Manufacturing	→	→	→	↘	↑
Mining	↗	↑	↗	↗	↑
Retail Trade	↑	→	↓	↗	↑
Services	→	↗	→	↗	↑
Transport, Communication, Utilities	↑	↑	↑	↘	↗
Wholesale Trade	↑	↑	↗	↘	↑

↑ Decreased Going Concerns (Improved)
↗ Moderately Improved (Less than 5% change)
→ Neutral
↘ Moderately Declined (Less than 5% change)
↓ Increased Going Concerns (Declined)

Figure 9

What happened that caused a decrease in going concerns in 2019 and 2020?

Despite economic uncertainty and pandemic-related operational impacts, the decrease in going concerns was not the result of a high company disappearance rate – i.e. companies that stopped filing or went bankrupt after receiving a previous going concern. There was an increase in the number of "clean" opinions issued, or opinions that improved a previous going concern. Simultaneously, new going concern opinions decreased. The number of companies that had received a going concern and subsequently disappeared remained stable in 2019 and decreased in 2020.



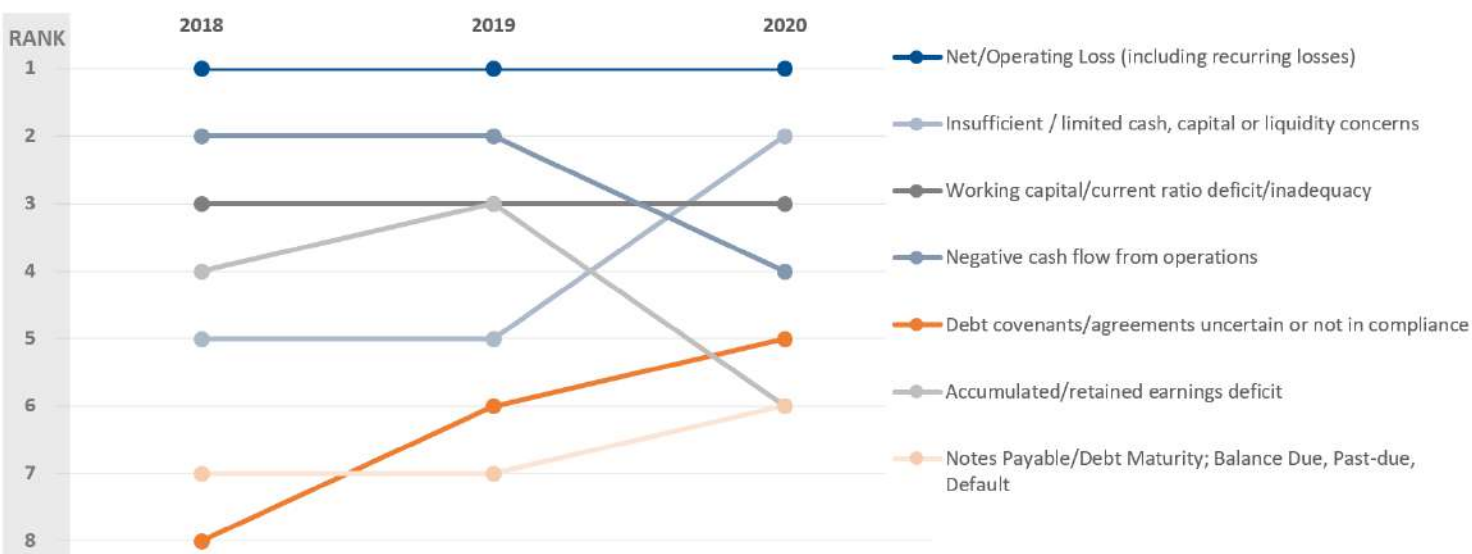
Issues related to debt covenants and notes payable/debt maturity were cited more prevalently in new going concern opinions in both 2019 and 2020 compared to 2018, indicating that these factors heightened the risk for more significant impacts on a company's financial condition, regardless of previous financial health.

The failure to meet debt covenant obligations and obtain financing was a significant risk during the pandemic due to the economic downturn and the uncertainty regarding the magnitude and timeline. For previously financially healthy companies that carried substantial debt covenant obligations pre-pandemic, COVID-19's impact on their financial position heightened the risk of failing to make required payments or violating agreements.

Figure 10

Most common issues cited in new going concern opinions

In 2019 and 2020, new going concern opinions citing issues related to debt covenants and notes payable/debt maturity increased to be the fifth and sixth most common issues cited. In comparison, for all going concerns between 2015 and 2020, notes payable/debt maturity and debt covenants were the tenth and eleventh most commonly cited issues. Insufficient cash / liquidity concerns also jumped in rank in 2020, climbing from the fifth most referenced issue to the second.



Impairments

KEY INSIGHT

The pandemic's impact on estimates contributed to $518 billion in write-downs related to asset values disclosed in 2020; charges related to PP&E were particularly costly. Impairments increased in terms of the number disclosed, the number of companies disclosing them, and aggregate charges, with more significant impacts on smaller companies.

The economic impacts and uncertainties of COVID-19 caused companies to re-evaluate the underlying fair value of company assets. The deteriorating macroeconomic factors during the pandemic, and associated declines in equity value, served as a triggering event for many companies, necessitating an interim impairment assessment to determine if assets were being overvalued.

This confluence of conditions during the pandemic served as a catalyst for impairments. The prevalence of triggered assessments, in addition to rote assessments, manifested a substantial number of disclosed impairments in both 2019 and 2020. Notably, the financial impacts of these write-downs exploded in 2020, nearly doubling 2019's aggregate impact and far surpassing the annual impairment totals disclosed in the previous five years.

In the case of very large write-downs, the need for a permanent adjustment to accurately reflect the underlying value of assets in response to the COVID-19 pandemic suggests that some of the changes were already needed. For example, if an asset needs to be impaired primarily due to destabilized estimates, it could be an indication the impairment is a result of ongoing problems at the company.

Figure 11

Impairment trends during COVID-19

The pandemic's impact on the economy affected the valuation of assets, as considerations and judgements used in impairment assessments were complicated by the uncertainty and volatility. In 2019 and 2020, there was an increase in the number of total disclosed impairments, unique companies disclosing an impairment, and aggregate impact amounts.

Figure 12

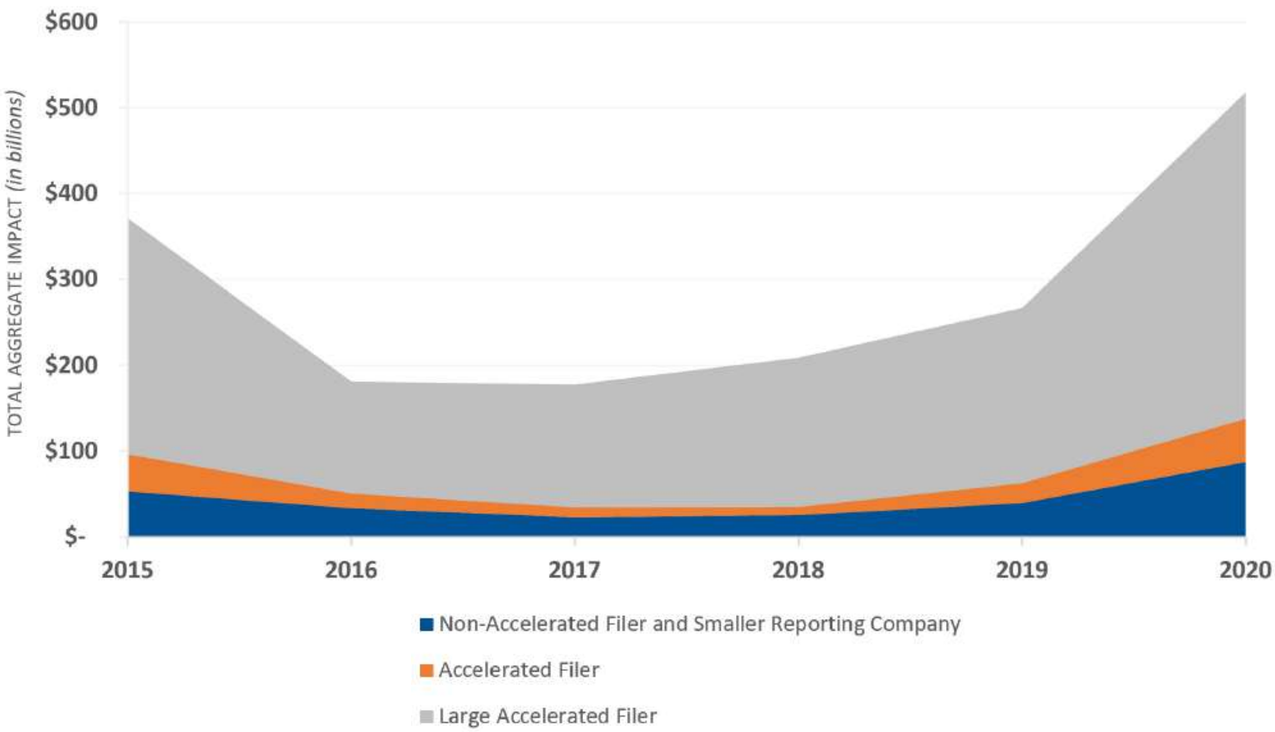
Impairment impacts in 2020, by company location

US-headquartered companies were responsible for 80% of 2020's aggregate disclosed impairment charges, resulting in $418 billion in asset write-downs. Foreign-headquartered companies, a smaller portion of the public company population, disclosed $102 billion in impairment charges; a quarter of that amount can be attributed to one very large PPE impairment taken by a Dutch energy company.

Figure 13

Impairment impact trends during COVID-19, by filer size

Impairment charges disclosed in 2020 significantly increased across companies of all sizes. Large Accelerated Filers experienced a significant jump in aggregate impairment charges, partially attributed to several massive impairments taken by large companies.



Despite several massive impairments disclosed by large companies, small companies, with less resources to mitigate the impacts from global disruption, are at a higher risk for impairments with the potential to cause long-term damage to their financial health.

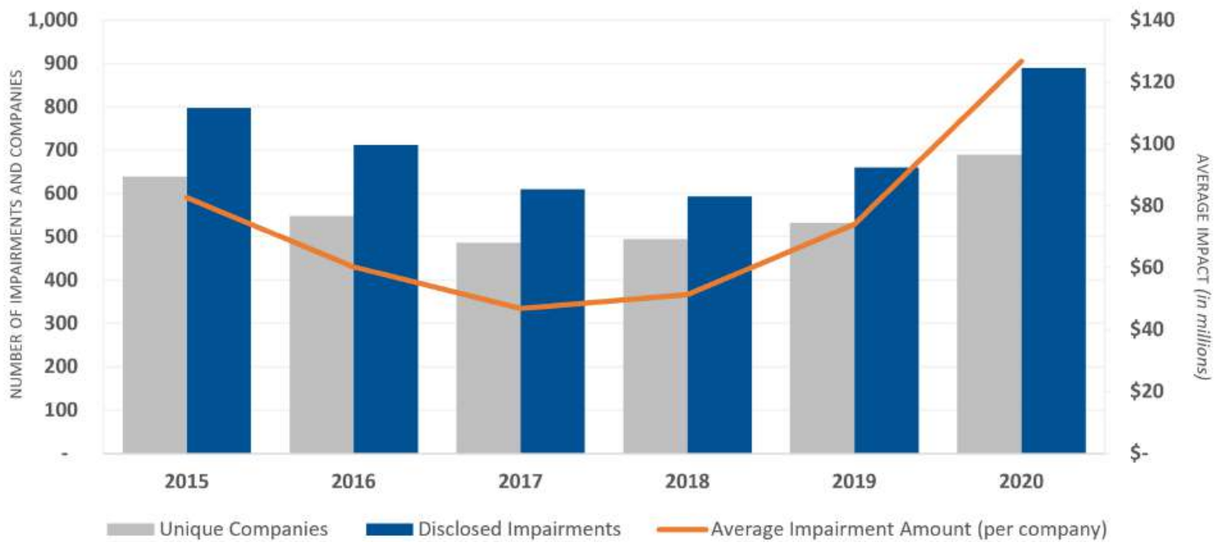
Under normal conditions, smaller companies are less likely to have a developed system of controls. Poor controls diminish accounting quality, heightening the risk for assets to be overstated and eventually need to be written-down.

In the setting of COVID-19, all companies were forced to grapple with added uncertainty when valuing assets. However, constrained resources and less robust control systems that exist at smaller companies further obscure management's ability to accurately predict when market and consumer disruptions will end, and the state of the economic environment in the aftermath. These conditions positioned smaller companies to experience tangible impacts on their financial health.

Figure 14

Impairment trends during COVID-19 for small companies

Non-Accelerated filers and Smaller Reporting Companies experienced a 35% increase in the number of impairments disclosed in 2020, indicating that the financial health of these entities was more negatively affected by the pandemic than the general population.



The estimates, assumptions, and future expectations underlying asset valuation models were substantially impacted by shifting trends during the pandemic, heightening the risk of needing to take an impairment charge.

Industries that rely on assumptions related to trends in consumer behavior and patterns were particularly impacted. For example, a retailer's assumption that certain changes in consumer behavior brought on by pandemic conditions - such as a shift to e-commerce - are likely to be long-term or permanent, would mean the value of the physical retail location needs to be written down.

Figure 15

Impairment trends during COVID-19, by industry

During 2019 and 2020, companies in the Retail Trade, Services, and Mining industries each disclosed aggregate impairment charges exceeding $100 billion. These industries were particularly susceptible to the pandemic-related changes to underlying estimates and assumptions .

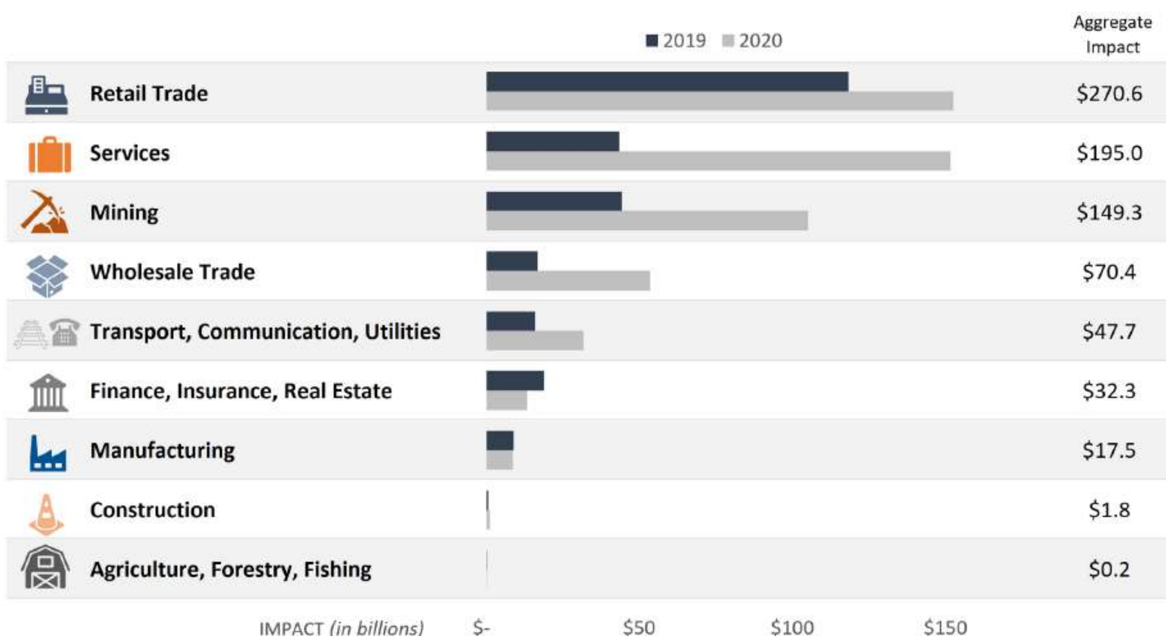
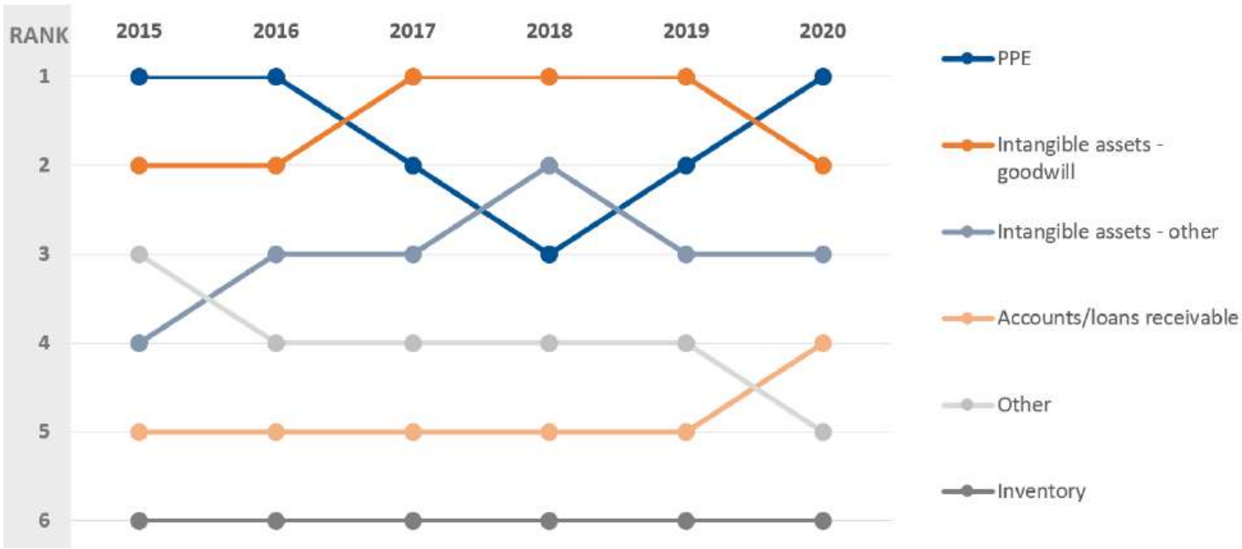


Figure 16

Impairment types, ranked by annual aggregate impact

The pandemic's impacts complicated estimates and forecasts underlying the valuation of long-held assets, in some cases substantially shifting long-held future expectations. Predictably, impairments related to property, plant, and equipment (PPE) became more costly in 2020, as the valuation of these assets are particularly sensitive to estimates of future pricing/utility.



Future Considerations

Restatements

The risk for a restatement is heightened during unprecedented circumstances such as those brought on by COVID-19. Interruptions to normal operations and rapid changes to the control environment provide an opportunity for weaknesses and errors.

In particular, changes related to personnel brought on by the pandemic heighten the risk for restatements. As of July 20, 2021, only seven restatements from six companies reference the pandemic as a contributing factor in the misstatement. It is possible that additional restatements will be disclosed, as the substantial nature of the changes that occurred, including a reduction in personnel and the transition to remote work, will continue to pose a risk.

Furthermore, the complex accounting associated with receiving federal pandemic relief funds, such as through the Paycheck Protection Program (PPP), presents additional opportunities for future misstatements.

Example 3

Control issues due to COVID-19 impacts will continue to heighten risk of restatement

Unique Fabricating, Inc.

"...the Company identified errors that were not detected as a result of the previously identified material weakness within certain controls and as a result the Company has concluded it is necessary to restate the Quarterly Reports on Form 10-Q for the Relevant Periods. The Company believes that the material weakness identified in its Annual Report on Form 10-K/A for the fiscal year ended December 29, 2019, which related to limited finance staffing levels that were not commensurate with the Company's complexity and its financial accounting and reporting requirements, combined with changes as a result of the COVID-19 pandemic, such as accounting and finance personnel working remotely, contributed to the errors and the failure of the Company to identify and correct the errors in a timely manner."

Enforcement

A crisis such as the COVID-19 pandemic opens the door for malfeasance and for bad actors to lure investors into scams. The SEC warned investors of these types of behaviors early on in the pandemic, issuing an Investor Alert for Frauds Targeting Main Street Investors in April 2020.[4]

Throughout the pandemic, the SEC charged companies and executives attempting to improperly profit from the global fear and uncertainty by making fraudulent claims to the public about their products and services. The SEC also targeted investment scams, charging multiple individuals and entities with committing pump-and-dump schemes on microcap company stocks during the pandemic.

There may be additional SEC enforcements in the future that stem from the pandemic, but accounting-related or FCPA investigations often take years to complete.

COMPANY	DATE	DESCRIPTION
ARRAYIT CORPORATION	June 2020	Fraudulent claims company developed a COVID-19 blood test.
APPLIED BIOSCIENCES CORP	May 2020	Fraudulent claims company would offer an at-home COVID-19 test.
DECISION DIAGNOSTICS CORP	December 2020	Fraudulent claims company developed a COVID-19 blood test.
PARALLAX HEALTH SCIENCES	July 2021	Fraudulent claims about availability of COVID-19 screening tests and PPE.
PRAXSYN CORPORATION	April 2020	Fraudulent claims related to ability to acquire and supply critical PPE.

4 Frauds Targeting Main Street Investors

Conclusion

In summary, the impacts from the COVID-19 pandemic significantly affected risks for public companies related to financial reporting, financial health, and future events.

FINANCIAL REPORTING

Lockdowns and work-from-home mandates impeded normal operating conditions and procedures.

- Late filings skyrocketed as many companies opted to take advantage of the SEC relief; however, the number of days companies actually required to file their late reports remained the same.
- Changes in controls were required for 800 companies to adapt to the pandemic conditions, while others already had controls and procedures in place to cope with the evolving circumstances.

FINANCIAL HEALTH

The economic uncertainty and shifting macroeconomic trends upended estimates.

- Minimal impact was noted on the prevalence of going concerns, apart from an increased reliance on debt and concerns over insufficient cash.
- The volatility's impact on asset valuation contributed to a staggering $518 billion in total impairments disclosed in 2020 – nearly double 2019's total.

FUTURE EVENTS

Risks in financial reporting will remain heightened.

- The rapid shift in company operations and procedures during the pandemic leaves room for material misstatements that have not been discovered.
- Going forward, additional scrutiny applied to disclosures and financial statements could result in future litigation or regulatory enforcement.

In conclusion, important insights about risks facing public companies, and risk management procedures, can be gained in the aftermath of this unprecedented global crisis. This informs best practices for the future to mitigate the impacts of an unanticipated event that significantly alters macroeconomic conditions.

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