KPMG

COVID-19 Impact by Accounting Standard

Reporting Update

31 March 2020, 20RU-005

Challenging current economic environment

The world is currently in the grips of the Coronavirus (COVID-19) pandemic. The spread of COVID-19 has resulted in significant disruption to business operations and increase in economic uncertainty, with increased market volatility and a marked decline in long-term interest rates in developed economies.

Current COVID-19 environment creating challenges for financial report preparers

Impact on financial statement preparation

As organisations take immediate actions to assess their exposure, positioning them to appropriately support key stakeholders, employees and customers, this pandemic is also likely to result in significant financial reporting implications for preparers of financial reports. The current conditions and events create an unprecedented level of uncertainty and risk for organisations which they will have to factor into their reporting to stakeholders.

Key considerations by standard prepared to assess potential impacts

Summary by accounting standard

Preparing your financial reports during this period can feel overwhelming as accounting impacts need to be considered across most aspects of the business. Many entities will have to reconsider numerous aspects of their financial reporting obligations, including those that may have been relatively static for several years. To assist you, KPMG has developed a summary of the key considerations by accounting standard which can be used as a reference by organisations to provide a checklist of the main considerations that may impact your financial statements in light of the current unfolding situation.

This list of considerations is not exhaustive. For a deeper dive into some of these accounting issues and considerations, including going concern implications, refer to our online Coronavirus: Financial Reporting Resource Centre (coming soon).

New KPMG financial reporting and audit resource centre launching soon with more guidance

Other reporting obligations

In addition to accounting standard implications, entities also have to consider their obligations under the Corporations Act, other relevant legislative arrangements, their constitutions as well as guidance and relief issued by regulators such as ASIC, APRA, ASX and ACNC (Not-for-profits). Our resource centre will also capture relevant guidance from Australian regulators and include information on how your statutory audit may be impacted. This website will continue to be updated as the situation develops.

If you have any questions, please reach out to your usual KPMG contact.

Accounting Standard	Accounting considerations
AASB 2 *Share-based Payments*	• If an entity's share based payment (SBP) arrangement has non-market vesting conditions (e.g. EBITDA hurdles), has there been a true-up for the number of instruments expected to vest based on whether the hurdles will be achieved? If a non-market vesting condition is no longer expected to be met, no cumulative SBP expense is recognised. In certain situations, this may result in a negative share based payment expense for the period. • If a SBP arrangement has market vesting conditions (e.g. TSR hurdles) or non-vesting conditions, have these conditions been appropriately reflected in the grant date fair value of the SBP arrangement? For existing equity-settled SBP arrangements, there will be no adjustment to reflect changes in expectation of whether market or non-vesting conditions will be met, that is, expenses are still recognised even though these awards may no longer be expected to vest. For cash-settled SBP arrangements, the liability is continually remeasured to fair value. • For changes made to existing SBP awards in light of COVID-19, such as reducing an EPS hurdle, or using discretion to allow vesting or to settle in equity rather than cash, has the impact on the accounting been considered? Changes to an award may result in a beneficial modification that needs to be accounted for as an additional expense over the remaining modified vesting period.
AASB 3 *Business combinations*	• Are there certain conditions precedent in sale and purchase agreements, such as obtaining third party financing, that have previously been considered non-substantive (i.e. procedural/ administrative), that are now considered substantive? If so, entities may need to reconsider whether control has been achieved. • For acquisitions that are still in the measurement period, if the acquisition took place before the occurrence of COVID-19, the fair value of assets and liabilities acquired should not be adjusted for the impact of COVID-19 as they do not represent conditions existing at the date of acquisition. For acquisition that took place after the occurrence of COVID-19, has the impact been appropriately reflected in the fair value of the acquired assets and liabilities? The estimate should reflect information that would have been reasonably available at acquisition date. • If an entity has outstanding contingent consideration from prior acquisitions, has the fair value of that contingent consideration been adjusted for the change in circumstances? Fair value changes in

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	contingent consideration that meets the definition of a financial liability should be recognised in profit or loss.
AASB 4 *Insurance contracts*	• See discussion below on AASB 1023 *General Insurance Contracts* & AASB 1038 *Life Insurance Contracts*.
AASB 5 *Non-current Assets Held for Sale and Discontinued Operations*	• If management changes its business strategy or restructures its business, do any assets or operations meet the definition of held for sale or discontinued operations? • If entities have previously classified non-current assets as held-for sale or an operation as discontinued operation, is a sale still considered to be highly probable and expected to be completed within 12 months of balance date? Any assets that are to be abandoned do not meet the held-for-sale requirements.
AASB 6 *Exploration for and Evaluation of Mineral Resources*	• Is the impact of COVID-19 an indicator of impairment for exploration and evaluation assets? For example, is substantive expenditure no longer budgeted or planned, or is the carrying amount of the exploration and evaluation asset unlikely to be recovered from successful development or by sale?
AASB 7 *Financial Instruments: Disclosures*	• Are there sufficient disclosures which will enable users to evaluate the impact of credit risk, market risk and liquidity risk? There are extensive disclosure requirements in AASB 7. For example: – How is the entity managing credit risk, liquidity risk and market risk in the current environment? – If there is concentration of risks, is there disclosure explaining how management determines concentrations, the shared characteristic for each concentration and the amount exposed to each shared characteristic? – What are the inputs, assumptions and information used to measure and manage credit losses? – For liquidity risk management, how is the entity managing disruptions to its cash flows including fulfilling its financial obligations?

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AASB 8 *Operating Segments*	• If a change in business strategy or restructuring has occurred, does this have an impact on the composition of operating segments? Where results are grouped and reported differently to the Chief Operating Decision Maker as a result of these changes, operating and reportable segments may change. In this case, comparative information will also need to be restated unless impracticable in which case current period segment disclosures are made under both the old and new basis of segmentation. A discontinued operation is not an operating or reportable segment.
AASB 9 *Financial Instruments*	• Impairment – Judgements and assumptions are applied to estimate the expected credit loss for financial assets. Past indicators and assumptions may no longer be applicable in the current environment. Entities need to reassess whether there has been a change in the risk of default over the *expected life* of the loan, and if there is, what is the probability the customer/borrower will default and what is the loss if there is a default? This should be based on reasonable and supportable information available to entities. Entities should consider the disclosure of information about the basis of inputs and assumptions that are being applied – See AASB 7: *Financial Instruments: Disclosures and* AASB 101 *Presentation of Financial Statements*. For financial services entities, some of considerations include: – Are the indicators for significant increase in credit risk (SICR) still appropriate? – Should the segmentation of portfolios be adjusted to reflect the impact of COVID-19 e.g. by industry/location/size? – Have multiple potential outcomes been considered e.g. periods of suspended operations and production, the time frame and speed over which the business is expected to recover, and other economic factors such as unemployment rates taking into consideration the impact of the government stimulus packages? – Are the outcomes based on external sources such as economists' forecasts? – Are there any debts that can be separately identified as impaired? If they are, they should be assessed individually. – Is the fair value of collateral updated?

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	– If the effects of COVID-19 cannot be reflected in existing models, how are inputs and economic assumptions applied to estimate the post-model overlays? • Some of the above considerations are also applicable to corporates that have a portfolio of trade or lease receivables. For example: – Should the portfolio of receivables be segmented based on the industry/location of their customers? – If an entity provides financial relief to its customers, is there an assessment of whether there is an increase in the risk of default by entities that apply for relief? – Have the use of multiple probability weighted potential outcomes been considered e.g. periods of suspended operations and production, the time frame and speed over which the business is expected to recover, and other economic factors such as unemployment rates taking into consideration the impact of the government stimulus packages? – Are the outcomes based on external sources such as economists' forecasts? – Are there any debts that are individually impaired? If there are, they should be assessed individually. The entity should also consider whether this is an indicator of an increase in the risk of default by other customers in a similar industry. – If the terms for future services are renegotiated, for example, lowering of rent, this may not impact the estimation of expected credit losses for existing receivables unless this is an indicator there is an increase in the risk of default by the customer. • Fair value – Refer to discussion on fair values under AASB 13 *Fair Value Measurement*. • Hedge accounting – If an entity hedges a highly probably forecast transaction which is now no longer expected to occur, has the hedge been discontinued and the change in fair value recognised in the income statement? The treatment of any amount in the cash flow hedge reserve would also need to be reassessed. – If a hedged item, e.g. future purchases or sales or future financing, is reduced or delayed, has a re-assessment of the hedge relationship been performed? This would generally give rise to

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	ineffectiveness and in certain circumstances, the change in fair value of the derivative, including the amount recognised in cash flow hedge reserve may have to be recognised in the profit or loss. • Classification of financial assets – Is there a change in the entity's business model regarding its financial assets (held-to-collect, held for sale and collect or held for sale)? If entities start selling financial assets that were previously classified as held-to-collect, are the reasons behind the sales still consistent with the designated business model? Selling assets from the held-to-collect portfolio does not automatically affect the classification of the remaining assets. • If an entity renegotiates the terms of its existing debt e.g. change in covenant requirements, extend its term or changes the payment structure, has it considered whether the change is a substantial modification? If it is a substantial modification, the previous debt including any capitalised transaction costs are derecognised, and a new debt instrument is recognised at fair value. Different guidance applies to financial assets and financial liabilities when assessing whether a modification is substantial. • If an entity has arrangements where the counterparty can call on it to make a margin payment when certain triggers are met, are margin call settlement liabilities appropriately recognised and measured? • If an entity has issued a financial guarantee, has it reassessed the measurement of the guarantee liability? Entities should apply the principles of expected credit losses to estimate the carrying amount of this guarantee liability.
AASB 10 *Consolidated Financial Statements*	• Do any control, joint control or significant influence assessments need to be reconsidered in light of COVID-19? Look out for: – Terms and conditions in contractual arrangements where control (i.e. power over the relevant activities and to a lesser extent, variability in returns) of an entity can be lost to other parties, such as financiers, in the event of a breach of contract driven by the deterioration in the financial condition of the entity. – Put or call options over investments in other entities that may become exercisable or terminated due to the current market conditions.

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AASB 11 *Joint Arrangements*	• See discussion on AASB 3 *Business Combinations*; AASB 10 *Consolidated Financial Statements*; AASB 128 *Investments in Associates and Joint Ventures* and AASB 136 *Impairment of Assets*
AASB 12 *Disclosures of Interests in Other Entities*	• See discussion on AASB 10 *Consolidated Financial Statements*; AASB 11 *Joint Arrangements* and AASB 128 *Investments in Associates and Joint Ventures.*
AASB 13 *Fair Value Measurement*	• For items quoted in an active market, the market price at measurement date provides the most reliable evidence of fair value. Fair value reflects the conditions and hence the value as at the measurement date. • If the item is not quoted in an active market, and the inputs significant to the valuation are unobservable (level 3 fair value), are the inputs and assumptions reflective of the market conditions and information available at measurement date? – Are the increased level of volatility and risks such as credit and liquidity reflected either in the cash flows or the discount rate? – Have valuation assumptions and inputs been updated for changes in the current market conditions? E.g. discount rates, sales prices and volumes, costs, taxes, inflation, foreign exchange rates. Adjusting for events after measurement date is not permitted unless they provide additional evidence of conditions that existed at the measurement date and these would have been reasonably available to market participants at that date. See AASB 110 *Events after the Reporting Period.* – Has the use of multiple probability weighted potential outcomes been considered e.g. periods of suspended operations and production, the time frame and speed over which the business is expected to recover, and other economic factors such as unemployment rates taking into account the impact of the government stimulus packages? – Are the outcomes based on external sources such as economists' forecasts?

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	– Has the impact of increased volatility and uncertainty been reflected in the determination of fair value? The discount rate should not double count the risk if it is already included in the cash flow forecasts. • AASB 13 includes extensive disclosure requirements. For example, if an item is a Level 3 fair value, is there sufficient quantitative information about the significant unobservable inputs?
AASB 15 *Revenue from Contracts with Customers*	• If a contract with a customer includes variable consideration (e.g. service level guarantees, performance fees, right of returns, implied price concessions), measures of progress and breakage estimates, have entities reconsidered the assumptions used in their measurement and recognition of revenue to reflect current market conditions? Updates to these estimates may result in a reversal of previously recognised revenue. • If any force majeure claims have been made against revenue contracts, has the effect been reflected in the amount of revenue recognised? • Have any customer contracts become onerous? (See discussion on AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* below) • If contracts with customers are renegotiated, have entities considered how the guidance on modifications to contracts would apply? • Consider implications of increased credit risk and contract enforceability on whether a contract for the purposes of revenue recognition still exists. If a contract for the purposes of AASB 15 does not exist, then revenue may need to be deferred. • If it is no longer likely that there will be future contracts with a customer, has the period of amortisation for capitalised costs been reconsidered? Expense recognition may be accelerated.
AASB 16 *Leases*	• If a lessee has changed the business strategy, e.g. it plans to close some sites, has management reassessed the lease term? If there is a change in a business decision that is directly relevant to whether it will terminate the lease, the lease liability is re-estimated taking into consideration any termination

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	penalties. The amount is calculated based on a revised discount rate at the date of reassessment. Any difference between the carrying amount and the new discounted amount is adjusted against the ROUA. • If a leased asset is no longer being used, has the right-of-use asset been assessed for impairment under AASB 136 *Impairment of Assets*? • If a lessee receives rental concessions from the lessor, has management considered whether there is a modification to the lease contract? Refer to KPMG's Lease modifications publication for guidance. If there is a decrease in scope, for example, a reduction in the leased asset or a decrease in term, there may be a profit or loss impact. • For a lessor, has it considered how a change in the lessee's circumstances (for example it is now unlikely to exercise an option to extend or it is no longer likely to exercise the purchase option at the end of the lease) impact the current lease accounting, including recoverability of either the underlying asset or the finance lease receivable? • If a lessor modifies an operating lease contract, it accounts for the modification as a new lease, and adjust its lease payments for any prepaid or accrued lease payments from the original lease. • If a lessor modifies a finance lease contract, is the new arrangement an operating lease or still a finance lease? If it is still a finance lease, the lessor apply AASB 9 *Financial Instruments* to the accounting of the lease receivables. If it is now an operating lease, it accounts for the modification as a new lease from the effective date of modification.
AASB 101 *Presentation of Financial Statements*	• If an entity is impacted by COVID-19, has the ability to continue as a going concern been considered? For example: – If profitability has fallen, is EBITDA sufficient to fund interest, investment and repayment of financial commitments? – Have covenants in loan documents been breached or are likely to be breached? – Have disposal of assets been contemplated to free up cash or eliminate losses? – Has there been a failed refinancing?

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	– Has there been a significant decrease in sales and/or an expected decrease in the ability to provide goods and services? – Have major suppliers been exerting pressure for payments? – Have there been negative profit warnings? – Have the implications of the Australian Government "Temporary Relief for Financially Distressed Businesses" been considered? The going concern assessment is assessed on the date the financial statements are authorised for issue. Material uncertainties relating to an entity's ability to continue as a going concern are required to be disclosed. • Current/ non-current classification of debt – Has the changed market conditions affected an entity's ability to meet its debt covenants? If an entity is in breach of a debt covenant, will this result in the debt being callable and hence classified as current? Entities should consider discussing potential future breaches of covenants with their financiers in advance of balance date to determine whether debt covenants can be adjusted or waived. • Significant judgements and estimates – Have disclosures been expanded as appropriate to include references to the uncertainty surrounding key accounting estimates and judgements and the potential impacts? For example, there is a greater level of estimation uncertainty relating to the determination of the recoverable amount of non-financial assets or cash generating units and expected credit losses on financial assets.
AASB 102 *Inventory*	• If entities have perishable inventory that cannot be distributed due to supply chain disruptions, or excess inventory due to a reduction in demand or force majeure claims, has the impact on net realisable value been considered? If significant write-downs of inventory are recognised, entities should consider whether this should be disclosed. • If additional costs are incurred due to disruptions and delays, an entity should consider whether these costs can be capitalised into the cost of inventory, or expensed as incurred?

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AASB 110 *Events after the Reporting Period*	• If an entity obtained information after reporting date regarding an estimate or judgement, the estimate or judgement should only be adjusted if the information indicates that it would have been reasonably available at the reporting date. • Refer to 20RU-003 *Coronavirus outbreak potential financial reporting impacts* for discussion on the impact of COVID-19 on 31 December 2019 financial statements.
AASB 112 *Income Taxes*	• If an entity has recognised deferred tax assets arising from tax losses, has the recoverability been reassessed given changing economic conditions? • If as a result of COVID-19, an entity reconsiders whether to distribute profits from subsidiaries, has the entity reassessed whether it is appropriate to recognise deferred tax liabilities associated with undistributed profits? • If an entity is granted income tax incentives by governments, have current and deferred taxes been adjusted to reflect this? Incentives granted by governments related to income taxes are only reflected in the measurement of current and deferred tax once they have been substantively enacted. • Where an entity's intention regarding the use of assets changes due to the current market conditions, does this have any implications for the tax base of these assets or applicable tax rates?
AASB 116 *Property Plant & Equipment*	• Have current market conditions resulted in a change to residual values or useful life to require a revision to depreciation rates? A change in depreciation rates represents a change in estimate under AASB 101 *Presentation of Financial Statements*. • If an asset is sitting idle, has the impact on depreciation been considered? Depreciation on idle assets continues unless a usage method of depreciation is applied, such as units of production. • If additional costs are incurred due to disruptions and delays, do these meet the capitalisation criteria, or are they expensed as incurred? • See discussion on impairment under AASB 136 *Impairment of Assets*.

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AASB 119 *Employee Benefits*	• If operations are being curtailed for a period of time, has the estimated timing of when employees are expected to take their leave entitlements been reassessed? The proportion of long service leave expected to be taken in the next 12 months could be significantly higher and/or the expected timing of annual leave may be bought forward. • If an entity has announced redundancies, have the appropriate termination benefits been recognised for those employees along with redundancy provisions given the strict recognition requirements for redundancies in the standard? • Defined benefit plans – Have assumptions such as discount rates been updated to reflect current economic conditions in the calculation of the obligation? At this stage, it is not expected that there will be any impact on life expectancies built into any modelling as the full impact is not yet known, however this should be monitored. It may also be relevant for entities preparing interim financial statements to consider whether to obtain a revaluation of their defined benefit obligations given the potentially material movements in valuations.
AASB 120 *Accounting for Government Grants and Disclosures of Government Assistance*	• If an entity is the recipient of a government grant which is required to be repaid if conditions attached are not met, has a reassessment of whether those conditions will be satisfied been performed? Consider whether there should be any adjustments to the cash flows in impairment models and to recognise a liability to repay the grant. • For any new stimulus related grants, ensure all terms and conditions are reviewed in determining the appropriate accounting. More guidance will be provided once details of these grants are known.
AASB 121 *The Effects of Changes in Foreign Exchange Rates*	• If an entity liquidates or abandons its interest in a foreign operation, has the impact on the foreign currency translation reserve been considered? Where an entity is deemed to have disposed of its foreign operation, any associated foreign currency translation reserve should be reclassified to profit or loss. • If a foreign operation has been written down or impaired, the related foreign currency translation reserve should not be reclassified to the profit or loss.

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AASB 123 *Borrowing Costs*	• If an entity ceases the active development of a qualifying asset for an extended period, has the entity considered suspending the capitalisation of borrowing costs?
AASB 127 *Separate Financial Statements*	• If an entity has investments in subsidiaries, associates or joint ventures held at cost or equity accounted, has the recoverability of those investments been considered in light of the deterioration in economic conditions? (See also discussion on impairment under AASB 136 *Impairment of Assets*). • If an entity holds investments in subsidiaries, associates or joint ventures at fair value, has the fair value been adjusted for the impacts of the current market conditions?
AASB 128 *Investments in Associates and Joint Ventures*	• See discussion on AASB 3 *Business Combinations*; AASB 10 *Consolidated Financial Statements* and AASB 136 *Impairment of Assets.*
AASB 133 *Earnings per Share*	• If the entity is now loss making, are potential ordinary shares still dilutive? Potential ordinary shares are only dilutive if they increase the loss per share from continuing operations.
AASB 134 *Interim Financial Reporting*	• Has the effect of significant changes in the market since the previous reporting period been considered when determining what disclosures should be included in the interim financial statements? The interim financial statements must include an explanation of events and transactions that are significant to an understanding of changes in the financial position and performance of the entity since the last reporting period. For example an entity may need to consider additional disclosures on significant judgements and estimates since the last annual reporting period, details of impairments, inventory write downs, loan defaults and renegotiations, and fair value measurements. • If management determines that a material uncertainty exists in relation to the entity's ability to continue as a going concern at the date the interim financial statements are authorised for issue, has that uncertainty been appropriately disclosed in the financial report?

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AASB 136 *Impairment of Assets*	• If an entity's market capitalisation falls below its net assets carrying amount, this is an indicator of impairment. As a result, it may be necessary to perform detailed impairment testing and determine the assets or cash generating units' recoverable amount. It is expected that many entities may be required to perform impairment testing as a result of the current market conditions. • Have the effects of COVID-19 been reflected in budgets and cash flow forecasts? Assumptions to consider include but are not limited to: – Any periods of suspended operations and production – The time frame and speed over which the business is expected to recover from COVID-19 – Ability to earn revenue from providing goods/services to customers, including the impact of potential disruption to distribution and production, for example due to supply chain issues or Government imposed shutdowns and trade restrictions – The use of multiple probability weighted cash flow outcomes. • If an entity used a discounted cash flow model to determine recoverable amount: – Have assumptions including discount rates and macro-economic assumptions such as inflation, exchange rates and commodity prices been updated for the effects of COVID-19? Consider involving specialists to determine appropriate assumptions. • Has the entity considered and reflected the increased volatility and uncertainty in impairment models? The discount rate should not double count the forecasting and market risks if they are already included in the cash flow forecasts. It would generally be expected that the discount rate will be higher than past rates to reflect higher risk and uncertainty.

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AASB 137 ***Provisions, Contingent Liabilities and Contingent Assets***	• Restructuring provisions – If an entity is planning to recognise a provision for restructuring, is there is a formal restructuring plan in place at balance date which has raised a valid expectation in those affected that the entity will carry out the plan? • Onerous contracts – If any contracts, in particular revenue contracts become onerous, due to the inability to source inputs and/or because of penalties from delays due to shutdowns etc., is it appropriate to recognise a provision for onerous contracts? • Has the exposure to potential litigation arising from force majeure claims not being accepted, COVID-19 infections traced to an entity's premises, employment contract issues etc. been considered? Entities should consider any litigation or claims that have come to their attention as a flow on from the outbreak and consider whether the impacts are appropriately disclosed as contingent liabilities or recognised as provisions. • If an entity has business continuity insurance and can recover some or all of the costs of closing down as a result of COVID-19, has an insurance recovery receivable been recognised if recovery is virtually certain or a contingent asset disclosed?
AASB 138 ***Intangible Assets***	• See discussion on Impairment of assets under AASB 136 *Impairment of Assets*.
AASB 140 ***Investment Property***	• In valuing investment properties at fair value, have management considered whether rental yields are still reasonable in an environment where many businesses are closing locations, or where valuations are based on turnover, the decline in turnover? • See discussion on fair value consideration under AASB 13 *Fair Value Measurement*.
AASB 141 ***Agriculture***	• If an entity has locked down or quarantined workforces, has the impact on production, crop yields and harvesting and other inputs been considered in valuing agricultural assets? Consider whether it is still appropriate to use the same assumptions about yields and other inputs in the valuations if, for example, normal level of fertilisation/ tending to crops has not been maintained. • See discussion on fair value consideration under AASB 13 *Fair Value Measurement*.

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AASB 1023 *General Insurance Contracts*	• Where COVID-19 is an insurable event, has the insurance liability been appropriately updated to reflect the expected impact of COVID-19 claims?
AASB 1038 *Life Insurance Contracts*	• Have assumptions such as discount rates been updated to reflect current economic conditions in the calculation of the insurance liability? It is not expected that there will be any impact on life expectancies built into any modelling as the full impact is not yet known, however this should be monitored.
AASB 1056 *Superannuation Entities*	• Defined benefit plans – Have assumptions such as discount rates been updated to reflect current economic conditions in the calculation of the obligation? At this stage, it is not expected that there will be any impact on life expectancies built into any modelling as the full impact is not yet known, however this should be monitored. It may also be relevant for entities preparing interim financial statements to consider whether to obtain a revaluation of their defined benefit obligations given the potentially material movements in valuations. • Refer to the discussion on Fair Value measurement under AASB 13 *Fair Value Measurement*.

Contacts

Patricia Stebbens
Partner
KPMG
+61 3 9288 6261
pstebbens@kpmg.com.au

Zuzana Paulech
Partner
KPMG
+61 2 9335 7329
zpaulech@kpmg.com.au

Kristen Haines
Senior Manager
KPMG
+61 3 9288 5184
khaines@kpmg.com.au

Hayley Pang
Senior Manager
KPMG
+61 8 9263 4818
hpang1@kpmg.com.au

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