MAB MAANDBLAD VOOR ACCOUNTANCY EN BEDRIJFSECONOMIE

Maandblad voor Accountancy en Bedrijfseconomie 95(11/12) (2021): 397–411
DOI 10.5117/mab.95.75536

Research Article

Effects of the COVID-19 pandemic on disclosures in passenger airlines' financial statements

Ralph ter Hoeven, Ymke Roosjen

Received 20 September 2021 | **Accepted** 13 November 2021 | **Published** 16 December 2021

Abstract

This article analyses the impact of COVID-19 on the disclosures of 24 financial statements of passenger airline companies in Europe (including United Kingdom), North America, China (including Hong Kong), Middle East and South America for financial year 2020. This impact is significant in our research sample as evidenced by a total revenue decrease of 60% compared to previous year. We have examined for specific areas whether the airline companies contribute to transparent reporting and useful information to existing and potential investors, regulators, supportive government bodies and other stakeholders following the COVID-19 pandemic. The areas of our research focus on going concern, rent concessions, significant judgements and estimates, impairments, governmental support and the auditor's report. Our study shows diversity in the extent of transparency in both financial statements and auditor's opinions. Good financial practices are included and discussed in this study to further stimulate transparency in corporate reporting.

Relevance for practice

This article is to the interest of users of the financial statement, auditors, standard setters and regulators. The research findings describe how airlines disclosed the effects of COVID-19 in their financial statements and how auditors responded in their auditor's report on the effects of COVID-19 in the airline industry. This paper includes several recommendations regarding the disclosure of tax relief, deferment of payments, lease concessions and going concern matters.

Keywords

COVID-19, airlines, state aid, going-concern, key audit matters, significant estimates and judgements, rent concessions and impairments

1. Introduction

The outbreak of Coronavirus disease of 2019 (COVID-19) pandemic is having a significant impact on the passenger airline industry. The total number of airline passengers dropped down due to travel restrictions, border closure and quarantine measures. The airline industry received more than USD 173 billion on support and relief from governmental bodies based on International Air Transport Association (IATA)[1] estimations up to 13 November 2020 (IATA 2020). Considering the development of the COVID-19 pandemic, the uncertainties in the industry and the support programs to airline companies, it is important that companies provide readers of the financial statement with useful and transparent information.

In this article we investigate 24 financial statements of airlines with shares listed on a regulated exchange for the year ending 31 December 2020 or 30 March 2021. The aim of this article is to evaluate the quality of disclosures stemming from the variety of COVID-19 support measures including the going concern section and several sections in the auditor's report including the key audit matter paragraph, the material uncertainty relating to going concern paragraph and the emphasis of matter paragraph.

We have confined our population to the passenger airline industry because this industry suffered unprecedently hard from the COVID-19 pandemic due to all travel restrictions issued by local governments affecting both tourist and business travel markets adversely. An overview of the population is presented in Appendix 1. The selection of the sample will be explained in Chapter three.

This article is structured as follows. In the next section, we will elaborate on some statements of supervisory authorities setting expectations for the disclosure quality in the financial statements related to the COVID-19 pandemic. We will use these expectations as a benchmark for our study. In section three we will further explain the sample selected.

Section four describes the outcomes of this study. The specific elements that will be analyzed in in this section are going concern, rent concessions, significant judgements and estimates, impairments, governmental support and the auditor's report. In the last section, conclusions are drawn, and recommendations are given.

2. Supervisory body expectations

In this section we will especially focus on issued reports of the financial reporting supervisory bodies that are overseeing the markets of our research sample. We verified especially the expectations communicated to market participants to create a benchmark for our empirical financial statement research.

The impact of the COVID-19 pandemic over the entire corporate sector is diverse in all aspects. Where some business sectors benefit from the developments (home food delivery, e-commerce), other sectors are heavily and adversely impacted. Among these, as explained in the introduction section, the passenger airline industry ranks high due to multiple restrictions and regulations that limited the free movement of individuals to restrain the spread of the virus. For corporate communication to investors this creates a challenge in terms of explaining transparently the impact of the pandemic on the financial health of the company. The European Securities and Market Authority (ESMA) stresses in its press announcement of its report on enforcement of corporate disclosure (6 April 2021) the need for a comprehensive presentation of the pandemic's effects on issuers activities which is important for both financial reporting and the provision of non-financial information.

ESMA issued earlier (28 October 2020) its annual Public Statement defining the European common enforcement priorities for 2020 annual reports of listed companies (ESMA 2020a). The common enforcement priorities related to International Financial Reporting Standards (IFRS) financial statements for the 2020 year were specifically impacted by the pandemic: International Accounting Standard (IAS) 1 presentation of financial statements (going concern assumption, significant estimates and judgements), IAS 36 impairment of assets and IFRS 16 leases. In its Public Statement of 20 May 2020, ESMA emphasized already the disclosure requirements for IAS 12 taxes and IAS 20 Accounting for Government Grants and disclosure of Government Assistance (ESMA 2020b).[2]

ESMA also underlines the responsibility of management and supervisory bodies including the importance of the oversight role of audit committees which is key to ensure the overall internal consistency of the annual financial report and contribute to high-quality annual financial reports (ESMA 2020a).

In the United States of America, the Division of Corporate Finance of the Security and Exchange Commission (SEC) issued specific disclosure guidance with respect to the pandemic (SEC 2020). SEC registrants need to consider which information related to COVID-19 should be included in other areas of SEC filings, such as Management, Discussion and Analysis or risk factors, in addition to the footnotes of the financial statements. Materiality, both qualitative and quantitative, and the surrounding specific facts and circumstances of companies will be important in this assessment of disclosing information. Companies are in this regard expected to disclose the effects of COVID-19 on the financial condition, liquidity position, outlook, valuation, and impairment of assets. Also, the SEC is encouraging disclosures that allow investors to evaluate the current and expected impact of COVID-19 through the eyes of management, and that companies proactively revise and update disclosures as facts and circumstances change. We will consider this disclosure guidance and encouragements comparable with the ESMA Public Statements.

3. Methodology/ Research

3.1. Sample

The Factiva database was consulted to identify the 100 largest listed airlines in the world based on the latest available market capitalization and the Dow Jones Industry Classification with the code airlines on 8 April 2021. The financial statements which were available as per 1 May 2021, either on the website of the airline or the website of the regulator, are included in this research. Furthermore, this study selected those financial statements that are prepared in accordance with IFRS-International Accounting Standard Board (IASB), IFRS-European Union (EU) or United States Generally Accepted Accounting Principles (US GAAP) and includes an auditor's report.

The main activity of the sample relates to passenger airline business given the unprecedented adverse impact of this specific industry. Airlines which have their main activities in cargo, lessor airline activities, airline manufacturing or private jet airlines were eliminated from the population to create a sample with comparable (adverse) market circumstances. Finally, airlines were selected with financial year reporting dates between 31 December 2020 and 31 March 2021 to analyze the effects of COVID-19 on the financial statements for a comparable period.

This resulted in a research population of 24 financial statements, 10 North American airlines, 8 European airlines (including the United Kingdom and Turkey), 3 Chinese airlines (including Hong Kong), 2 Middle East airlines and 1 airline from South America. The total assets of this sample amounts to €505.652 million and the total equity amounts to €59.062 million. For further details regarding the names of the companies and financial data, we refer to appendix 1. We conclude with the observation from appendix 1 that the total revenue of the population decreased with 60% compared to the previous year which illustrates the enormous impact of COVID-19 for this specific industry.

3.2. Accounting principles and auditing standards used

The population consists of airlines which apply either IFRS (as published by the IASB and/or endorsed by the EU) or US-GAAP. We analyze in this section whether the sets of standards are comparable for the elements we include in our study.

The specific elements compared for the accounting standards are going concern, rent concessions, significant judgements and estimates, impairments and governmental support, and auditor's opinion.

Under both accounting standards going concern needs to be disclosed in the financial statements when there is significant doubt on it (IAS 1.25 & Accounting Standards Codification (ASC) 205-40-50-1).

International Financial Reporting Standards prescribes that significant judgements and estimates should be disclosed (IAS 1.122 & IAS 1.125). US-SEC registrants should provide a discussion of critical accounting policies and estimates as part of item 303 (Management's discussion and analysis of financial condition and results of operations) of Regulation S-K.

In this research we pay attention to governmental support which could be governmental assistance (IAS 20), a form of relief or deferment of income tax payments (IAS 12) or funding (IAS 32/ IFRS 9). The US accounting standards do not provide specific guidance for governmental grants to profit entities but refers to ASC 958 (Not-for-Profit-entities) in which disclosure requirements are given for contributed (non)-financial assets which are comparable with requirements given in IAS 20 paragraph 39. In the United States a $2.2 trillion economic stimulus bill was signed into law on March 27, 2020, in response to the economic fallout of the COVID-19 pandemic. This CARES (Coronavirus Aid, Relief, and Economic Security) Act included specific provisions to provide payments to passenger air carriers amounting to a maximum of $25 billion that had to be exclusively used for the continuation of payment of employee wages, salaries, and benefits. In addition, the CARES Act also provides assistance in the form of loans, grants, tax credits, or other forms of government aid. The accounting treatment of these programs follows the same principles as in IFRS with the most important distinction whether the transaction with the government is an exchange transaction (a reciprocal transfer in which each party receives and pays commensurate value) or a contribution. This will determine whether the scope of the program is in IFRS 9 (e.g. funding), IAS 12 (income tax relief) or IAS 20 (non-reciprocal government support), a combination[3] or the US-GAAP equivalents of these standards. It is obvious that the nature of the program or transaction with the government should be disclosed under both IFRS and US-GAAP.

The Financial Accounting Standard Board (FASB) staff issued a question and answer (Q&A) in which guidance is provided for rent concessions which do not qualify for a lease modification. This FASB staff question-and-answer document focuses on the application of the lease guidance in Topic 842, Leases for lease concessions related to the effects of the COVID-19 pandemic. For concessions related to the effects of the COVID-19 pandemic, an entity will not have to analyze each contract to determine whether enforceable rights and obligations for concessions exist in the contract and can *elect* to apply or not apply the lease modification guidance to those contracts. On 28 May 2020, the IASB issued a similar election (a practical expedient) but only for lessees. According to this expedient a lessee may elect not to assess whether a COVID-19 related rent concession is a lease modification (IFRS 16.46A, IASB 2020). This option or expedient will allow rent concessions to be recognized in the period to which the concession relates. If the normal modification stipulations would have been followed the concessions would often have been spread over the remainder of the lease period. Thus, by making use of the expedient a better matching could be reached between the benefits of the rent concessions (for lessees) and the adverse financial effects caused by the pandemic.

Regarding the determination of impairment of goodwill, intangible and tangible assets guidance differs between US-GAAP and IFRS. According to US-GAAP an entity uses a two-step impairment testing model for tangible assets and finite-lived intangibles, while under IFRS, an entity must use a one-step model. Under both sets of standards, an entity must use a one-step model for testing goodwill and indefinite-lived intangible assets; however, under US-GAAP, an entity can use an *optional qualitative assessment*. Under both IFRS Standards and US-GAAP, assets may be tested as a group or individually, depending on whether largely independent cash flows attributable to the assets exist. The groupings may differ under IFRS Standards and US-GAAP owing to how they are defined.

If we consider the most important research topic of this study, the quality of disclosures, it is important to note that the impairment *disclosures* for goodwill, intangible and tangible assets are comparable between US-GAAP (ASC 350 and ASC 360) and IFRS (IAS 36). Given the differences in setting up the impairment test, it could be theoretically possible that an airline company reporting under US-GAAP would not record an impairment loss due to the qualitative assessment, not existing under IFRS, and therefore will not have to disclose any impairment loss. However, a qualitative assessment means that an entity is permitted to first assess qualitative factors to determine *whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount.* It is obvious that this assessment during the pandemic crisis would fail, meaning that the entity is obliged to perform a quantitative impairment test that would also be required if IAS 36 would have been applied.

Given the fact that we might expect impairment losses for economically similar airline companies under both GAAPs and considering the similarity of impairment disclosures for goodwill, intangible assets and tangible assets, we consider US-GAAP and IFRS comparable for the aim of this study.

Regarding the auditor's opinion the International Auditing and Assurance Standards Board (IAASB) and Public Company Accounting Oversight Board (PCAOB) request the auditor to disclose matters which are material to the financial statements and have a subjective or complex auditor judgement (International Standard on Auditing (ISA)706 and Auditing Standards (AS) 3101). Also, the auditor's responsibilities in the audit of financial statements, relating to management's use of the going concern assumption in the preparation of the financial statements, under which adding a going concern related emphasis of matter paragraph to the unqualified opinion, are comparable (ISA 570, AS 2415).

Though in literature it is admitted that the scope of a PCAOB/AS 3101 'critical audit matter' (CAM) could be more narrow than a key audit matter (KAM) under ISA 706 (Jermakowicz et al. 2018), we conclude that both key audit matters and critical accounting matters emphasize the elements of the financial statements which are critical for the reader The impact of COVID-19 is without any doubt a critical or key audit matter related to auditing accounts or disclosures that are material to the financial statements. Hence, we consider these two sources of guidance comparable for the aim of this research.

4. Results

4.1. Going-concern paragraph, auditor's opinion and significant judgements and estimates.

As indicated earlier, the passenger airline companies are situated in a distressed environment. The responsibility of the auditor to report on going-concern related uncertainties is expected to be challenging in these circumstances. If an auditor issues an unqualified audit opinion and/or refrains from issuing a going concern emphasized audit opinion and the audited company subsequently fails, the cost to the auditor in terms of increased litigation costs and loss of reputation are often substantial (Carcello and Palmrose 1994; Geiger et al. 2020). In this research, we focus on how many airlines include a going-concern paragraph in accordance with IAS 1.125 or ASC 205-40-50. Subsequently, we compare whether the auditor included a material uncertainty relating to going concern (MURG) in his opinion when the financial statements contain a paragraph in which material uncertainties related to going concern are included.

The disclosure of key audit matters (KAMs) is an important section of the auditor's opinion and is relevant for the users of financial statements (Gold and Heilman 2019). Auditors should carefully weigh which matters they disclose as *key* audit matters in their reports. We expect that COVID-19 related matters will be identified as key audit matters.

We further note regulators identified recommendations on the auditor's report and going concern paragraph, e.g., the Royal Netherlands Institute of Chartered Accountants (NBA 2020). Also, the PCAOB states that the significance of the impact of COVID-19 may warrant including additional elements in the auditor's report, such as explanatory language or an explanatory paragraph when there is substantial doubt about the ability of the company to continue as going concern (PCAOB 2020).

Finally, in line with (Brouwer et al. 2016), we will investigate, in the context of the COVID-19 matters, the (two sided) relationship between identified key audit matters in the auditor's opinion and the significant judgements and estimates paragraph in the financial statements. One might expect that COVID-19 matters identified as KAM are also included in the significant judgements and estimates section. This expectation also holds for the other direction. Once identified as a *significant* judgement or estimate, we might assume that this matter is rather part of the key audit matter section.

4.1.1. Going concern paragraph

In our population 22 financial statements include a separate paragraph on going concern or a paragraph on the consequences of COVID-19 and two financial statements do not.

In Table 1 an overview is provided with the frequency of occurrence of five topics we observed in the going concern or COVID-19 paragraph.

Table 1. Going concern

Topics disclosed in the going-concern or COVID-19 paragraph	Percentage of the sample (%)
Governmental support	75.0%
Compliance debt covenant as per year-end or in the year afterwards	12.5%
Changes in credit rating	4.2%
Cash position and liquidity monitoring	54.2%
Scenario analysis for the near future	16.7%

In 18 financial statements airlines elaborated on whether they received governmental support in the specific going concern or COVID-19 paragraph. In four remaining financial statements, governmental support is not described in these specific paragraphs. However, in three out of these four financial statements a disclosure of governmental support is provided elsewhere in the financial statements. One company did not disclose whether any governmental support was received at all.

Five financial statements explicitly elaborate on their covenants in the specific going concern or COVID-19 paragraph. Two financial statements disclose in this paragraph that they do not meet the covenants as per year end. Two companies disclose that they will meet the covenants in the coming 12 months based on the current forecasts. One company discloses that covenants will possibly be breached in the second quarter of 2021 under the base case scenario. According to these financial statements, it does not affect the going concern assumption as per year end, because an available credit facility was not drawn per year-end.

One airline elaborated on the change in its credit rating explicitly in the specific going concern or COVID-19 paragraph.

Thirteen financial statements included their cash position in the specific going concern or COVID-19 paragraph. One other company included a reference from the going concern paragraph to the paragraph relating to financial risk management and fair value.

Four financial statements disclose in the specific going concern or COVID-19 paragraph that management applied scenario analyses in assessing whether the going concern assumption could be applied. All these four financial statements have been prepared in accordance with IFRS.

We found the best practice for the going concern or COVID-19 paragraph in the financial statements of Finnair Oyj.[4] The company has disclosed multiple scenarios for the expected capacity and recovery of the market. The liquidity position and the possibility of breaching a specific covenant in the second quarter of 2021 have been explained, including the consequences for the going concern assessment. Management describes how they have determined that the financial statements should still be prepared based on the going concern assumption. As a result, the disclosure is a detailed company specific analysis of the going concern situation.

4.1.2. Auditor's opinion

Notably, the auditors of all 24 financial statements issued an unqualified auditor's opinion. Two auditors' opinions included a MURG paragraph, and two auditors included an emphasis of matter paragraph (EoM)[5] in their auditors' opinion. We would expect that based on ISA 570/AS 2415 only a MURG paragraph would have been used for the material uncertainties caused by COVID-19 to continue as a going concern. One of these four auditors added an additional EoM for a financial reorganization process

Figure 1. Elements of the going concern paragraph of Finnair Oyj, Annual report 2020, page 51. https://investors.finnair.com/~/media/Files/F/Finnair-IR/documents/en/reports-and-presentation/2021/annual-report-2020.pdf

> The main differences between the scenarios relate to the timing of the demand recovery, unit revenue development and development of customer demand. In the optimistic scenario, the demand recovery is expected to materially start in June 2021 and in July 2021, Finnair expects to operate around 60% of its capacity (measured in available seat kilometres) as compared to 2019. In the base case scenario, which is considered as the most probable of the three, the recovery is expected to materially start in August 2021 and the capacity would be around 70% of the 2019 levels in September 2021. In the pessimistic scenario, the start of the recovery would be expected to materially take place in October 2021 and the capacity to remain below 80% of the 2019 levels in November 2021. Under each of the scenarios, the business is expected to return to the operational levels (measured in available seat kilometres) comparable to 2019 in year 2023. All of the management forecast scenarios are based on the development of passenger demand and capacity levels that depend on the implementation of the vaccination programs, lifting of travel restrictions and global acceptance of vaccine passports. It is assumed in all scenarios, that the unit revenue (RASK) will remain below the 2019 levels throughout the period of the business plan due to lower passenger volumes and lower share of corporate travel. In the base case scenario, the passenger load factors and thus also the unit revenue would recover slower in 2021 than in the optimistic scenario, but faster than in the pessimistic scenario. At the same time, the committed cost saving program included in the scenarios will decrease unit costs. Flight related variable expenses depend on the planned capacity, whereas aircraft maintenance investments are assumed to stay rather constant between all scenarios.
>
> In 2020, Finnair took immediate and decisive action to mitigate the negative impacts relating to the COVID-19 pandemic by adjusting its operations and targeting both temporary and permanent cost reductions. The temporary measures include temporary layoffs of employees, limiting spending only to the mandatory and compliance driven items and the temporary grounding of a large part of its fleet in order to accommodate its cost base to lower level of operations until the demand for flying returns again. On 28 October 2020, Finnair announced that it is targeting 140 million euro in permanent cost base reductions (as compared to year 2019) by 2022. As part of the mentioned cost savings program, Finnair has finalized significant co-operation negotiations which resulted in a reduction of ca. 600 jobs.
>
> In addition to the operational measures, Finnair responded quickly in order to secure adequate funding to support its liquidity. Finnair's refinancing plan included e.g. raising 500 million euro of new equity through a rights issue, drawdown of 600 million euro pension premium loan, refinancing of the company's outstanding 200 million euro hybrid note, three refinancing transactions related to A350 aircraft and rescheduling of future aircraft deliveries to later periods.
>
> As a result of the aforementioned actions, Finnair's liquidity position remained strong and as at 31 December 2020, the Group held liquid funds of 792.2 million euro (481.7). The cash funds including other current financial assets (maturity over 3 months) totalled to 823.7 million euro (952.7). The Group management and the Board of Directors continue to pay close attention to the Group's cash position considering the challenging dynamics in its current operating environment that are negatively impacting the Group's cash flows. Based on Finnair's current estimate (base case scenario), the covenant terms related to Finnair's undrawn 175 million euro revolving credit facility are estimated to be possibly breached during the second quarter of 2021. The credit facility is not in use as at the date of preparation of the financial statements and Finnair's financing during the going concern assessment period is not dependent on the existence of the facility. Finnair plans to initiate negotiations with the syndicate banks with respect to covenant amendments. The maturities of the Group's interest-bearing liabilities are presented in note 3.3. and information about the existing covenants, changes in hedging policies and management of liquidity risk is described in notes 3.4, 3.5 and 3.8.

Figure 2. Material uncertainty relating to the going concern assumption in the auditor's opinion relating to the financial statements of International Consolidated Airlines SA, Annual report 2020, page 2. https://www.iairgroup.com/~/media/Files/I/IAG/AGM%202021/English/7%20May%20upload/2020_consolidated_annual_accounts_management_report_and_audit_report.pdf

> We draw attention to Note 2 of the consolidated financial statements which discloses the significant impact on the Group's results and cash flows caused by the COVID-19 pandemic.
>
> In its assessment of going concern, the Group have modelled two scenarios, the Base Case and the Downside Case. The Base Case takes into account the Board's and management's views on the anticipated impact and recovery from the COVID-19 pandemic on the Group and overall business across the going concern period. The Downside Case applies further stress to the Base Case to model a more prolonged downturn, with a deeper and more gradual recovery relative to the Base Case.
>
> The Directors of the Company have a reasonable expectation that the Group has sufficient liquidity to continue in operational existence for the foreseeable future and hence continue to adopt the going concern basis in preparing the financial statements. However, as disclosed in Note 2, in the event that a more severe downside scenario than those the Directors have considered were to occur the Group will need to secure sufficient additional funding which represents a material uncertainty that could cast significant doubt upon the Group's ability to continue as going concern. Our opinion has not been modified in this regard.

under 'Chapter 11' of the United States bankruptcy law. We observed that this airline filed for a Chapter 11 reorganization in the United States on 28 January 2021.

Two auditors referred in their MURG paragraph of their opinion to the going concern paragraph in the financial statements. The auditor of the International Consolidated Airlines Group SA financial statements[6] highlights in his opinion that directors of the company are working with two scenarios for analyzing the going concern assumption. We selected this as best practice, because it emphasizes which elements of the going concern assumptions are the most important according to the auditor, refer to Figure 2.

Given the fact that 22 companies include COVID-19 related matters in the separate paragraph on going concern, it is remarkable that 18 auditor's opinions do not include a material uncertainty relating to the going concern or emphasis of matter paragraph. Such a paragraph does not alter or modify the unqualified opinion but is only used by the auditor to *highlight a disclosure in respect of a material uncertainty in respect of going concern* (ISA 570/AS 2415). A possible explanation to not include this going concern reference might be that in the key audit matter section of his opinion (see next section) the auditor already specifically refers to COVID-19 related uncertainties. However, the next section shows that this explanation does only partially hold given the limited number of COVID-19 related matters. Another explanation might be the uncertainty related to the going concern is not material enough or the hurdle to add such going concern paragraph is still considered high given the assumed negative signal that the auditor reflects to the market (with the fear of causing more distrust in the company's financial position). But then the question arises: if even in these very adverse, pandemic related, economic conditions a going concern paragraph is not added, which situations (even more adverse) would then trigger this paragraph?

4.1.3. Key audit matters

As mentioned earlier, supervisory bodies have communicated their expectations on the effects of COVID-19 on the auditor's opinion. However, only five auditor's opinions include a key audit matter (KAM) that specifically relates to COVID-19. Also, the number of times an auditor uses the wording COVID-19 in a specific KAM is quite limited.

The sample shows a variation in the number of KAMs identified with a minimum of one and a maximum of nine. The total number of KAMs presented in this population is 73. Table 2 shows an overview of KAMs which are presented, how many times and whether a reference is made to COVID-19 in the specific KAM.

Table 2. Key audit matters

Key audit matters (KAMs)	Number of KAMs	COVID-19 mentioned
Revenue recognition and liability loyalty program	18	3
(In)tangible asset valuation including goodwill	18	6
Component accounting of aircraft and accrual of lease return cost	8	3
Implication of COVID-19 on the going concern	5	5
Recoverability of operating carry forward losses	5	1
Valuation of derivatives and effectiveness of hedging	5	3
Employee benefit plans	4	0
Accounting for state-aid funding (loans and/or equity) and conditions	3	3
Accounting for state aid reimbursement costs	2	2
Restructuring	2	2
Recoverability of aircraft maintenance deposits	1	0
Litigation and claims	1	0
First time adoption of IFRS 16	1	0

Each reported key audit matter counts as one in this table except for Hawaiian Holdings Inc. This company disclosed separately a key audit matter for impairment of goodwill and impairment of long-lived assets. In Table 2 this is counted as one key audit matter since we observed that other auditors disclosed this key audit matter on an aggregated level.

Most of the key audit matters relate to accounts with a high degree of estimate or judgement which is depending on future scenarios including future travel restrictions, border closure and quarantine measures.

As mentioned earlier in the previous paragraph, 22 airlines included a going concern paragraph in the financial statements and in four cases auditors emphasized the going concern paragraph in their report. In addition, Table

2 shows that five auditors addressed going concern as a key audit matter. As noted, it is remarkable that in thirteen cases the auditors do not mention or emphasize the going concern in their auditor's report given the severe distressful circumstances in the passenger airline industry.

Five key audit matters are dedicated to the complexity of accounting for state-aid which is the result of COVID-19 related support programs by governments. Four auditors mentioned employee benefit obligations as key audit matter due to the complexity of determining the fair value of plan assets and the measurement of defined benefit obligations. This audit matter is unrelated to COVID-19 as they were also repeatedly identified in previous financial statements. Two auditors pointed out restructurings due to COVID-19.

The key audit matters related to litigations, claims and first-time adoption IFRS 16 are not linked to COVID-19 in the auditors' report.

We have selected the auditor's report included in the financial statements of International Consolidated Airlines Group SA as best practice. The auditor has distinguished regular key audit matters from key audit matters with a significant impact on the financial statements resulting from COVID-19. It shows that valuation of financial instruments including hedging instruments, the workforce (restructuring), loss of revenue (governmental support), net operating losses and finance arrangement have been significantly affected by the COVID-19 outbreak. On top of that, the auditor described performed audit procedures for these COVID-19 related key audit matters. This shows how the auditor responded to these risks, see Figure 3.

4.1.4. Significant judgements and estimates

According to IAS 1.122 an entity shall disclose judgements management has made in the process of applying entity's accounting policies and that have the most significant effect on the amounts recognized in the financial statements. In paragraph 125 of IAS 1 a similar disclosure is required for sources of estimation uncertainty (from now on: estimates). According to the standard the judgements and estimates should be presented separately.

Therefore, it is remarkable that only International Consolidated Airline Group SA distinguishes significant judgements from estimates in its financial statements. Apparently, companies and their auditors have difficulty in separating these disclosure requirements, possibly because of the notion that also an estimation uncertainty arises from applying a policy. However, this is not how the IASB has meant it to be. For instance, application of the going concern principle is related to the application of a policy that requires judgement. In nature this is different from the estimation uncertainty surrounding (for example) the credit loss allowance for trade debtors. Consequently, the remaining 23 financial statements do not distinguish significant judgements from estimates. The

Figure 3. COVID-19 related key audit matters in the auditor's opinion for the financial statements of International Consolidated Airlines Group SA, Annual report 2020, page 5–6. https://www.iairgroup.com/~/media/Files/I/IAG/AGM%202021/English/7%20May%20upload/2020_consolidated_annual_accounts_management_report_and_audit_report.pdf

Other matters related to the impact of the COVID-19 pandemic

During 2020, the Group has been impacted by the COVID-19 pandemic with significantly reduced operating capacity. The impact on the business and the measures taken by the Group to preserve cash, resulted in a number of significant accounting matters. Other than as described in the key audit matters above, we identified the following material impacts on the financial statements.

Valuation of financial instruments and hedge effectiveness - The Group hedges its exposures to movements in commodity prices and foreign currency rates. The COVID-19 pandemic resulted in a significant decline in the price of oil and a significant reduction in the forecast fuel usage from the reduced flying schedule, which resulted in significant losses on the Group's derivative contracts. This resulted in charge to the income statement of €1,756 million. We focused on this area because of the significant judgement exercised by management in determining the revised estimates of jet fuel usage and foreign currency payments, the reassessment of hedge effectiveness and the material impact on the financial results of the Group.

Restructuring – The Group implemented restructuring programmes to reduce the employee base to align with the reduced size of operations in the revised business plans. Given the scale of the restructuring programmes and the number of individuals impacted, there is a risk the restructuring provisions were not recognized in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

Recognition of income from government support schemes – The Group utilized several measures announced by the UK, Spanish and Irish governments to provide assistance during COVID-19. There is a risk that the criteria of IAS 20 Accounting for Government Grants and Disclosure of Government Assistance have not been met.

Recoverability of deferred tax assets – The Group recognized deferred tax assets of €1.075 million and unrecognized deferred tax assets of €1.275 million. Due to the significant impact of the COVID-19 pandemic and the related uncertainty, there is a risk that the deferred tax assets recognized may not be recoverable.

Compliance with conditions pursuant to new financing arrangements – in order to secure its cash position and protect its liquidity despite the uncertainty of the COVID-19 pandemic; in addition to the Rights Issue, the Group has entered into financing arrangements with Spain's Instituto de Crédito Official (ICO), the UK's Coronavirus Corporate Finance Facility (CCFF) and the Ireland's Strategy Investment Fund (ISIF). These arrangements require compliance with certain conditions that otherwise would lead to the early repayment or cancellation of such facilities. The Group assesses its expected future finance position as well as other expected future transactions that could comprise their compliance with these conditions, triggering the early repayment or cancellation of these facilities.

minimum number of items of significant judgement and estimates is three and the maximum number is thirteen. An overview of the identified significant judgements and estimates is presented in Table 3.

Table 3. Significant estimates and judgements

Significant estimates and judgements	Number of financial statements
Impairment of (in)tangible assets including goodwill	23
Loyalty program and revenue recognition	22
Taxes/ Recoverability of operating carry forward losses	17
Return obligations airplanes	13
Employee benefit obligations	12
Useful life property, plant and equipment	8
Valuation of derivatives and effectiveness of hedging	7
IFRS 16: lease term	6
Expected credit losses (IFRS 9)	6
Fair value (IFRS 13 and ASC 820)	5
IFRS 16: discount rate	4
Provision spare parts and inventories	3
Litigations	3
Accrual for aircraft flying costs	2
Accounting of state aid (IAS 12 versus IAS 20)	1
Accounting of state aid funding (IAS 32)	1
Other *)	6

*) Other significant estimates and judgements are only remarked once and consider the following topics: provision, aircraft maintenance deposits, classification current versus non-current, classification of financial assets, fair value of financial instruments and investment of subsidiary.

Table 4. Separate disclosure of significant judgements

Significant judgements	Number of judgements
Engineering and other aircraft costs (maintenance provision)	1
Lease term of contracts with renewal and termination options (IFRS 16)	1

We identified 139 items in Table 3 and two items in Table 4. Most of the significant estimates and judgement topics are related to topics which are not new and were already indicated in previous year(s).

New accounting estimates and judgements which can be linked to the COVID-19 pandemic are operating grants and funding (state aid) in the financial statements of Turk Hava Yollari AO and SAS AB. The auditor of SAS AB linked a key audit matter to this significant estimate and judgement. The auditor of Turk Hava Yollari AO did not. Remarkable is the proactive attitude of the auditors of Deutsche Lufthansa AG and International Consolidated Airlines Group SA who added both two key audit matters to governmental support. One key audit matter for the way of funding and one key audit matter for the reimbursement of costs considering the complexity, size, and relevance of the matter. The airlines themselves did not identify these as significant judgements or estimates. Considering the enormous impact of governmental support and complexity it remains unclear why only a limited number of airlines and auditors expressed this as a significant estimate or judgement or identified it as a key audit matter.

As it turns out in Table 3 and Table 4 that only state aid accounting is a new significant estimate and judgement, we refer to the next paragraph for the best practice related to governmental assistance and income taxes disclosure.

4.2. Governmental assistance and income taxes.

The financial statements which are prepared on US GAAP are all headquartered in the United States of America. Based on the CARES Act, the US government provided for specific time periods tax reliefs for passenger airline ticket taxes, social security contributions, extension of tax compensating net operating losses to the preceding periods (tax loss carry backs), fuel taxes and federal transportation taxes.

The identification of which tax support programs are applicable for the financial statements based on IFRS in our research sample is more complicated because the airlines are widespread over different (tax) jurisdictions. For this reason, we have identified categories based on disclosure requirements in IAS 12, IAS 20, and IAS 32.

We categorized the support of governmental support in four categories: governmental guarantees, governmental tax relief or deferment, operating grant(s), and governmental loans, refer to Table 5 for a complete overview.

Table 5. Governmental support programs

Subject	Number of financial statements	EUR million
Governmental guarantees for continuing flight routes	4	EUR 1.791
Governmental tax relief or deferment	14	EUR 5.401
Operating grant	18	EUR 17.382
Governmental loan	14	EUR 19.301

We observe that four airlines recognized governmental income which was provided to *guarantee* certain flight routes in China (three airlines) and one for air services by SAS airlines for domestic routes in Norway. We cannot determine whether these are directly linked to COVID-19, but we consider it almost certain that this support would not have been provided without COVID-19. We understand that the CARES Act was also endorsed to guarantee the continuation of certain flight routes, but the governmental support related to this support program was not separately disclosed in the nine US GAAP financial statements included in our sample.

The airlines reported in fourteen cases that they received governmental tax relief or a deferment of taxes. The latter means that companies are allowed to pay current taxes at a later period as to improve the liquidity position. Nine of these financial statements are based on US GAAP standards and five financial statements are based on IFRS. Nine out of the fourteen airlines have disclosed the amount of this tax relief or deferment in their financial statements of which eight are based on US GAAP and one financial statement is based on IFRS. We cannot determine whether the financial statements have disclosed information of all material tax deferments or tax reliefs. We observe that the US GAAP financial statements only reported on one or certain elements of the tax reliefs of the CARES Act. It could be the case that certain elements are not material.

Ten financial statements did not disclose tax relief or deferment of taxes. All these ten airlines reported under IFRS. We observe that one of these airlines did not recognize or disclose taxes at all in their financial statements. Taxes depend on the local laws and regulations of the specific jurisdiction. We conclude that the tax disclosure on relief or deferment can be further improved from a qualitative and quantitative perspective.

In Table 5 the governmental loan consists of the loans between the airlines and the government including the governmental loan facilities to the extent drawn as per year end. We observe that fourteen airlines have drawn governmental loans or loans which are guaranteed fully or partially by the state for a total amount of EUR 19.301 million per year end. This means that there could be undrawn government loans (facilities) as per year end as well. All airlines which drew governmental or governmental guaranteed loans as per year-end included a disclosure related to terms and conditions of the loans. All US GAAP financial statements referred to the CARES Act or partially disclosed the most important elements and support conditions attached to these loans such as: payment of employees, restriction of furloughs over certain time periods, maintaining a certain level of commercial flights, prohibition of repurchase of shares over a certain time period, limitation of dividend over a certain time period, restrictions on remuneration of the board and the issuance of warrants in return for loans obtained from the US government. Aegan Airlines SA based in Greece, also disclosed the issuance of warrants for governmental loans in their financial statements.

We noted that no sustainability criteria were mentioned as a condition for obtaining the loans within the US GAAP financials statements. Air France-KLM mentioned as a condition for the Dutch governmental loan that the airline needs to become more sustainable. SAS AB describes that dividend payments need to be aligned with long-term sustainability goals and are depending on the conditions of the governmental support received for the COVID-19 pandemic.

Regarding four IFRS financial statements we observe that airlines which originate from international mergers received governmental loans from multiple countries. The terms and conditions are described in the financial statements per jurisdiction.

A remarkable observation stems from the financial statements of Aegan Airlines SA. The Chairman of the Board and the CEO decided and announced on 31 March 2020, that they will not receive any remuneration (both fixed and variable) for their services to the Company for 2020.

We have selected the financial statements of Spirit Airlines Inc.[7] as best practice for disclosing the nature and impact of governmental assistance, refer to Figure 4. The central disclosure of all governmental measures under the header COVID-19 legislation makes it understandable for the reader what the impact of governmental support is on the financial statements, both in current and future periods. The user of the financial statements can read the airline received forms of support such as a reimbursement for employee costs, a 10-year interest loan (including the issuance of warrants to the US federal government), refundable tax credits for employment taxes, certain tax loss carrybacks, waiver for federal fuel taxes and deferred payment of employer portion of social security taxes. More important is that the airline disclosed the related amounts to these programs and the financial statement affected or made a reference to the relevant note. Also, the restrictions for these governmental support programs are summarized.

4.3. Leases

Both the IASB and the FASB issued a practical expedient or relief for COVID-19 related rent concessions. The practical expedient provides lessees with an exemption from assessing whether COVID-19 related rent concessions is a lease modification. According to IFRS 16:60 '*An entity shall disclose the amount recognized in profit or loss for the reporting period to reflect changes in lease payments that arise from rent concessions to which the lessee has applied the practical expedient in paragraph 46A*.'

This research verifies how many financial statements in our sample make use of this practical expedient and whether the financial statements quantify the effect of the practical expedient for IFRS financial statements. Under US GAAP the practical relief was part of a staff Q&A document which requires no specific obligatory disclosure for this practical relief in the financial statements. We observe that the practical expedient or relief is not mentioned at all in the financial statements of twenty airlines. We cannot determine whether the practical expedient or relief is not used, not material enough to disclose or that the company is deficient in making the disclosure. An explanation for the six companies in our sample that report on IFRS as endorsed by the EU, might be that the European Union endorsed the IFRS 16 practical expedient after the issuance of the half year interim financial statements. As a result, the expedient could not be used in the interim financial statements. And subsequently, the companies did not choose to apply for the expedient in reporting year 2020 covering this interim period. The EU-endorsement process apparently hampers application of these 'quick fixes' in the standards. The same may apply to other jurisdictions that have endorsement processes before amendments to IFRS might be used.

Four airlines quantified the effect of the practical expedient for rent concessions due to COVID-19 in their financial statements. The range lies between EUR 0.4 million and EUR 22.3 million. Three financial statements disclose the effect of the practical expedient on the profit and loss account for a total value of EUR 3.2 million as required by IFRS 16.60A.

Figure 4. Best practice disclosure for governmental support programs in the financial statements of Spirit Airlines Inc. Annual report 2020, Form 10-K, page 51–53. 0001498710-21-000020 (q4cdn.com)

In April 2020, we entered into a Payroll Support Program ("PSP") Agreement with the United States Department of Treasury ("Treasury") pursuant to which we received a total of $344.4 million, used exclusively to pay for salaries, wages and benefits for our Team Members through September 30, 2020. Of that amount $73.3 million is in the form of a low-interest 10-year loan. In addition, in connection with its participation in the PSP, we issued to Treasury warrants pursuant to a warrant agreement to purchase up to 520,797 shares of our common stock at a strike price of $14.08 per share (the closing price for the shares of our common stock on April 9, 2020) with a fair value of $3.9 million. The remaining amount of $267.2 million is in the form of a grant and was recognized in special charges and credits, net of related costs, in our consolidated statement of operations. Refer to "Notes to the Consolidated Financial statements – Note 5, Special Charges and Credits" for additional information.
Pursuant to the warrant agreement with the Treasury, we registered the resale of the warrants and the 520,797 shares of common stock issuable upon exercise of such warrants in September and October 2020. Total warrants issued represents less than 1% of the outstanding shares of our common stock as of December 31, 2020. Refer to "Notes of the Consolidated Financial Statements –14 Debts and Other Obligations" for additional information on the notes issued and "Notes to the Consolidated Financial Statements – 11, Common Stock and Preferred Stock "for additional information on the warrants.

In connection with our participations in the PSP, we were, and continue to be subject to certain restrictions and limitations, including but not limited to:

- Restrictions on payment of dividends and stock buybacks through September 30, 2021;
- Limits on certain executive compensation including limiting pay increases and severance pay or other benefits upon terminations, through March 24, 2022;
- Requirements to maintain certain levels of scheduled services (including to destinations where there may be currently significant reduced or no demand) through September 30, 2020;
- A prohibition on reducing the sales, wages, or benefits of our employees (other than our executive officers or independent contracts, or as otherwise permitted under the term of the PSP) through September 30, 2020;
- Limitations on the use of the grant funds exclusively for the continuation of payment of employee wages, salaries and benefits; and
- Additional reporting and recordkeeping requirements relating to the CARES Act funds.

On April 29, 2020, we applied for additional funds under the Treasury's loan program under the CARES Act ("Loan Program"). On July 1, 2020, we executed a non-binding letter of intent with the Treasury which summarized the principal terms of the financing request submitted by us to the Treasury. In September 2020, we decided that we would not participate in the Treasury's loan program as we were able to secure other forms of financing described below. On December 27, 2020, the Consolidated Appropriation Act, 2021 was signed into law. This new legislation provides an extension or additional benefits designed to address the continuing economic fallout from the COVID-19 pandemic. The bill extends the PSP program of the CARES Act through March 31, 2021 ("PSP2") and provides an additional $15 billion to fund the PSP2 program for employees of passenger air carriers. In late December, we notified the Treasury of our intent to participate in the PSP2 agreement. We entered into a new payroll support program agreement with Treasury on January 15, 2021. We expect to receive approximately $184.5 million pursuant to our participation in the PSP2 program. In January 2021, we received the first installment of $92.2 million in the form of a grant. Of the remaining amount, we expect that approximately $25 million will be in the form of a low-interest 10-year loan. In addition, in connection with our participation in the PSP2, we expect to issue to Treasury warrants to purchase up to 103,761 shares of our common stock at a strike price of $24.42 (the closing price of the shares of our common stock on December 24, 2020).

In connection with our participation in the PSP2, we are subject to certain restrictions and limitations, including, but not limited to:

- Restrictions on payment of dividends and stock buybacks through March 31, 2022;
- Limits on executive compensation through October 1, 2022;
- Restrictions from conducting furloughs or reducing pay rates and benefits from March 31, 2021;
- Requirements to maintain certain levels of scheduled services through 1 March, 2022;
- Reporting requirements; and
- A reclass of employees that were involuntarily furloughed or terminated between October 1, 2020 and the carrier enters into the new payroll support agreement with the Treasury. Such employees, if returning to work, must be compensated for lost pay and benefits between December 1, 2020 and the date of such new payroll support agreement.

The Consolidated Appropriations Act, 2021 also extends and expands the availability of the CARES Employee Retention credit through June 30, 2021, however, certain provisions apply only after December 31, 2020. This new legislation amends the employee retention credit to be equal to 70% of qualified wages paid the employees after December 31, 2020, and before July 1, 2021. During the first two quarters of 2021, a maximum of $10,000 in qualified wages for each employee per calendar quarter may be counted in determining the 70% credit. Therefore, the maximum tax credit that can be claimed by an eligible employer in 2021 is $7,000 per employee per calendar quarter for the first and second quarters of 2021.
The CARES Act also provides for certain tax loss carrybacks and a waiver on federal fuel taxes through December 31, 2020, we had recognized $142.0 million in federal related tax loss carrybacks and $6.5 million in federal fuel tax savings reflected within aircraft fuel in our consolidated statements of operations.

Finally, the CARES Act also provides for deferred payment of employer portion of social security taxes through the end of 2020, with 50% of the deferred amount due December 31, 2021, and the remaining 50% due December 31, 2022. As of December 31, 2020, we had deferred $23.2 million in social security tax payments. The deferred amounts are recorded within other current liabilities and withing deferred gain and other long-term liabilities on our consolidated balance sheet.

Figure 5. Best practice disclosure for the COVID-19 rent relief practical expedient IFRS 16 in the financial statement of China Eastern Airlines Inc., Form 20-F, page F14. https://www.sec.gov/Archives/edgar/data/0001030475/000119312521135351/d39685d20f.htm

Amendment to IFRS 16 provides a practical expedient for lessees to elect not to apply lease modification accounting for rent concessions arising as a direct consequence of the COVID-19 pandemic. The practical expedient applies only to rent concessions occurring as a direct consequence of the pandemic and only if (i) the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change; (ii) any reduction in lease payments affects only payments originally due on or before June 30, 2021; and (iii) there is no substantive change to other terms and conditions of the lease. The amendment is effective for annual periods beginning on or after June 1, 2020 with earlier application permitted and shall be applied retrospectively.

During the year ended December 31, 2020, certain monthly lease payments for the leases of the Group's buildings, aircraft and engines have been reduced or waived by the lessors upon reducing the scale of production as a result of the pandemic and there are no other changes to the terms of the leases. The Group has early adopted the amendment on January 1, 2020 and elected not to apply lease modification accounting for all rent concessions granted by the lessors as a result of the pandemic during the year ended December 31, 2020. Accordingly, a reduction in the lease payments arising from the rent concessions of RMB3 million has been accounted for as a variable lease payment by derecognizing part of the lease liabilities and crediting to profit or loss for the year ended 31 December 2020.

The best practice for the disclosure on practical expedient for the lease concession can be found in the financial statements of China Eastern Airlines Inc, refer to Figure 5. The disclosure illustrates as per when China Eastern Airlines Inc.[8] applies the practical expedient, what kind of leases it covers, quantifies the effect of the practical expedient in a monetary value and explains the accounting policy used.

4.4. Impairments

As already mentioned, the SEC and ESMA requested clarity on impairments of assets especially during the COVID-19 pandemic given the severe impact on certain business sectors. In Table 6 we give an overview of impairment losses recognized in our research per category of asset.

Table 6. Impairments

Subject	Number of financial statements	EUR million
Impairment of goodwill	4	3.445
Impairment of other intangible assets	8	173
Impairment tangible assets	16	9.214
Impairment of other tangible assets	4	120
Impairment of leases (IFRS 16 and operating leases ASC 842)	7	571
Total		**13.523**

Table 6 shows an amount of EUR 13.523 million in total for impairment losses recognized in all categories which averages approximately 2,5% of the value of total assets in our research sample. This percentage shows that the total effect of impairments is still modest given the fact that the remaining 97,5% of the assets is still deemed recoverable despite the pandemic impact. The impairment tests are predominantly done by performing a *value in use method* as described in IAS 36. In this method estimates of future cash inflows and outflows of the cash generating unit to which the assets belong are derived from continuing use of the asset during its expected useful life and from its ultimate disposal. In the airline industry tangible assets have typically a long-term remaining average useful life. Therefore, assumptions about the post-pandemic recovery of the passenger airline industry are pivotal in these value in use tests. An expected quick recovery to pre-pandemic figures will probably not lead to material impairment losses in a value in use model while a slow recovery path of (for example) five years to normal pre-pandemic levels will probably have a material effect on recoverable amounts.

We have examined whether and how companies disclosed 'pandemic recovery scenarios' in their notes where the value in use assumptions are explained (based on IAS 36/ASC 350/ASC 360).

We observe that nine out of the 24 financial statements disclose aspects of the impairment test in the notes of their financial statements. Only three out of these nine financial statements discussed the recovery scenarios for the value in use calculation explicitly in the note of the impairment test.

The best practice for the impairment disclosure can be found in the financial statements of Finnair Oyj, refer to Figure 6. The disclosure illustrates what the period is for the forecast, whether different scenarios have been considered and how much weight is allocated to each scenario for the value in use calculation. Key assumptions have been benchmarked against external sources and a sensitivity check has been performed and disclosed, for a full overview of the disclosure related to impairment testing refer to pages 67 and 68 of the financial statements of Finnair Oyj.

5. Conclusion and Recommendations

The effects of the COVID-19 pandemic are drastic for the passenger airline industry as evidenced by the 60% decrease in revenue over 2020 compared to the previous reporting year. As the adverse economic conditions may cast significant doubt upon the airline's ability to continue as a going concern, we examined the content of the going concern paragraph in the financial statements. 22 airlines

Figure 6. Best practice disclosure of recovery scenarios in the value of use calculation in the financial statements of Finnair Oyj, Annual report 2020, page 68. https://investors.finnair.com/~/media/Files/F/Finnair-IR/documents/en/reports-and-presentation/2021/annual-report-2020.pdf

The value in use measurement is based on discounted cash flow model where the cash flow projections are based on the latest management forecast, covering a five-year period. The cash flows beyond the five-year period are projected to increase in line with management's long-term growth assumptions. In order to consider the uncertainty caused by the current COVID-19 pandemic and the future outlook, Finnair is utilizing the expected cash flow approach which is using multiple, probability-weighted cash flow projections based on the three different forecast scenarios prepared by the management. The scenarios and probabilities allocated to each scenario have been reviewed and approved by the Board of Directors. When determining the probabilities, the management has reflected on the uncertainty related to the COVID-19 vaccination timetable, lifting of traveling restrictions and other factors affecting the demand. The optimistic scenario, where the demand recovery is expected to materially start in June 2021, is considered to have a probability weight of 5%. The base case scenario, where the recovery is expected to materially start in August 2021, is considered to have 55% probability. The pessimistic scenario with the start of the recovery taking place in October 2021, is given probability weight of 40%. Under each scenario, the business is expected to return to operational levels (measured in available seat kilometers) comparable to 2019 in year 2023.

Key assumptions used in impairment review

	Dec 31, 2020	Sep 30, 2020	June 30, 2020
Discount rate (post-tax long-term weighted average cost of capital), %	**8.2**	**8.4**	**8.4**
Discount rate (pre-tax, derived from the long-term weighted average cost of capital) %	**9.3**	**9.5**	**9.8**
Long-term growth rate, %	**2.4**	**2.4**	**2.4**
Fuel cost range per ton (USD)	**540–610**	**500–615**	**520–650**

included a COVID-19 or going concern paragraph. It is unclear for us why the two remaining airlines did not include a going concern paragraph. In the auditor's opinions only four auditors added to their unqualified opinion an additional paragraph emphasizing the going concern disclosure in the financial statements. In addition, five auditors addressed the going concern uncertainty as part of their key audit matters. We would have expected more emphasizes of going concern matters in the auditor's opinions given the auditing standards (ISA 570/AS 2415) that are applicable. Further investigation is necessary to explain why auditors do not respond to the going concern paragraph in the financial statements.

The airlines identified state aid accounting in extremely limited cases as significant judgement and estimates which is also remarkable given the fact that judgement might be applied in the accounting for the diversity of support programs airlines received. For example, whether the programs are tax relief (IAS 12) based or related to government grants as defined in IAS 20. Judgement might also be applied in determining the benefit of a government loan or facility granted at below market terms.

Most of the financial statements include a tax disclosure on deferment or tax relief due to COVID-19. Less than the majority of the financial statements quantified the effects of tax deferment and tax reliefs. We observe that airlines disclose elements of deferment or tax relief. It remains unclear whether a complete overview of deferment or tax relief is provided to the users of the financial statement. We recommend airlines to be more transparent in the reporting of tax deferments and tax reliefs since this transparency is important in analyzing the effective tax rate of the company.

Although new practical expedient or relief provide lessees the opportunity to make use of rent relief due to COVID-19, only a small minority of the airlines discloses the quantitative and qualitative effects of the practical expedient or relief of rent concessions in their financial statements. The endorsement processes in jurisdictions like the European Union might hamper the use of these IFRS amendments that aim to be applied quickly.

Despite the drastic effect of the pandemic on the revenues of the airline companies in our sample. 97,5% of the assets is still deemed recoverable. The impairment of 2,5% of total assets at reporting date was predominantly caused by impairments of goodwill and tangible assets. Only three airlines expressed pandemic recovery scenarios of their value in use calculation in their financial statements. An improvement in the impairment disclosure is necessary to provide users of the financial statements with an overview of significant assumptions used in impairment testing.

Overall, we observe a large variation in the detail of disclosures that relates to the impact of the pandemic. Many companies still have generic disclosures that do not reflect companies' specific situations. Of course, a restriction to our observation is that we only examined a worldwide sample of 24 financial statements. This research population is relatively small and should not be used for extrapolation over wider populations. However, we have selected best practices in this article that are examples of more specific and tailored disclosures based on current circumstances and conditions. Hopefully, these disclosures will serve as a contribution to further transparency.

An area for further research is the application of ISA 570/AS 2415 regarding the disclosure of material uncertainty relating to going concern. It has not been used by the auditors in 18 of the 22 financial statements that included a going concern disclosure note. Such an additional paragraph does not alter or modify the unqualified opinion but is only used by the auditor to highlight a disclosure in respect of a material uncertainty regarding going concern. The reason this paragraph is not added is intriguing and cannot be derived from our financial statement desk research. Thus, we recommend this as an area that is worth further examination by applying other research methods like interviews.

- **Prof. dr. R.L. (Ralph) ter Hoeven RA** is professor financial accounting at the University of Groningen and partner in the professional practice department of Deloitte Accountants.
- **Y.C.E. (Ymke) Roosjen MSc RA** is specialist senior manager in the professional practice department of Deloitte Accountants.

Notes

1. The International Air Transport Association (IATA) supports aviation with global standards for airline safety, security, efficiency and sustainability. It is the trade association for the world's airlines.
2. The enforcement matters for non-financial matters, IFRS 9 Financial instruments and IFRS 7 Financial instruments will not be further discussed in this research.
3. We refer to IAS 20.10A for an example (government loan at a below-market rate of interest).
4. For a full overview of the disclosure related going concern refer to page 51 of the financial statements of Finnair Oyj. annual-report-2020.pdf (finnair.com).
5. Emphasis of matter paragraph is a paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements (ISA 706). For the going concern emphasis of matter, specific guidance is included in ISA 570 Going Concern. Where the auditor judges that going concern disclosures in the financial statements are adequate, the auditor might use a 'Material Uncertainty Related to Going Concern'. This acts in a similar way to an emphasis of matter paragraph but is only used by the auditor to highlight a disclosure in respect of a material uncertainty in respect of going concern.
6. The emphasis of matter in the auditor's opinion related to the financial statements of international consolidated airlines can be found on page 214 of the financial statements. iag-annual-report-and-accounts-2020.pdf (iairgroup.com).
7. The best practice for governmental support can be found on page 51, 52 and 53 of the financial statements. Annual Reports & Proxies - Spirit Airlines, Inc.
8. This is included on page 120 of the financial statements of China Eastern Airlines. 2021042701934.pdf (hkexnews.hk).

Literature

- Brouwer A, Eimers P, Langendijk H (2016) The relationship between key audit matters in the new auditor's report and the risk reported in the management report and the estimates and judgements in the notes to the financial statements. Maandblad voor Accountancy en Bedrijfseconomie 90(12): 580–613. https://doi.org/10.5117/mab.90.31228
- Carcello JV, Palmrose Z-V (1994) Auditor litigation and modified reporting on bankrupt clients. Journal of Accounting Research 32(supplement): 1–30. https://doi.org/10.2307/2491436
- Deloitte (2021) Roadmap. Comparing IFRS Standards and U.S. GAAP: Bridging the Differences (October 2021). https://www.iasplus.com/en/publications/us/ifrs-gaap-comparison
- Deloitte (2020) Highlights of the CARES act. https://www.iasplus.com/en/publications/us/heads-up/2020/issue-8
- ESMA [European Securities and Market Authority] (2020a) European common enforcement priorities for 2020 annual financial reports. ESMA32-63-1041. https://www.esma.europa.eu/sites/default/files/library/esma32-63-1041_public_statement_on_the_european_common_enforcement_priorities_2020.pdf
- ESMA [European Securities and Market Authority] (2020b) Public Statement: Implications of the COVID-19 outbreak on the half-yearly financial reports. ESMA32-63-972. https://www.esma.europa.eu/sites/default/files/library/esma32-63-972_public_statement_on_half-yearly_financial_reports_in_relation_to_covid-19.pdf
- ESMA [European Securities and Market Authority] (2021) ESMA publishes 2020 report on enforcement of corporate disclosure. ESMA71-99-1629. https://www.esma.europa.eu/press-news/esma-news/esma-publishes-2020-report-enforcement-corporate-disclosure
- Geiger MA, Gold A, Wallage P (2020) A synthesis of research on auditor reporting on going concern uncertainty: an update and extension. Working paper 2017A01. Foundation for Auditing Research. https://foundationforauditingresearch.org/files/papers/a-synthesis-of-research-on-auditor-reporting-on-going-concern-uncertainty.pdf
- Gold A, Heilman M (2019) The consequences of disclosing key audit matters (KAMS); A review of the academic literature. Maandblad voor Accountancy en Bedrijfseconomie 93(1/2): 5–14. https://doi.org/10.5117/mab.93.29496
- IATA [International Air Transport Association] (2020) Deep losses continue into 2021. https://www.iata.org/en/pressroom/pr/2020-11-24-01/
- IASB [International Accounting Standards Board] (2020) IASB issues amendment to IFRS Standard on leases to help lessees accounting for COVID-19 related rent concessions. https://www.ifrs.org/news-and-events/news/2020/05/iasb-issues-amendments-to-ifrs-standard-on-leases/
- Jermakowicz EK, Epstein B, Ramamoorti S (2018) CAM versus KAM—A Distinction without a Difference? Making Judgments in

Reporting Critical Audit Matters. The CPA Journal 88(2): 34–40. https://www.cpajournal.com/2018/02/19/cam-versus-kam-distinction-without-difference/
- NBA [Koninklijke Nederlandse Beroepsorganisatie van Accountants] (2020) Impact Coronavirus op accountantswerkzaamheden. NBA Alert 42, 6 april 2020. https://www.nba.nl/globalassets/wet--en-regelgeving/nba-alerts/alert-42/nba-alert-42-impact-coronavirus-update-6-april-2020.pdf
- PCAOB [Public Company Accounting Oversight Board] (2017) AS 3101: The auditor's report on an audit of financial statements when the auditor expresses an unqualified opinion, 2017-001. https://pcaobus.org/oversight/standards/auditing-standards/details/AS3101
- PCAOB [Public Company Accounting Oversight Board] (2020) COVID-19: reminders for audits nearing completion – spotlight. https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/documents/covid-19-spotlight.pdf?sfvrsn=24e6b033_0
- SEC [U.S. Securities and Exchange Commission] (2020) (COVID-19), Division of Corporate Finance Securities and Exchange Commission, CF disclosure Coronavirus Guidance: Topic no. 9. https://www.sec.gov/corpfin/coronavirus-covid-19
- SEC [U.S. Securities and Exchange Commission] (2020) Coronavirus (COVID-19), Division of Corporate Finance Securities and Exchange Commission, CF disclosure Guidance: Topic no. 9. SEC (United States of America). covid-19-spotlight.pdf [azureedge.net]

Appendix 1: Research sample

#	Name of the airline	Accounting Standard	Presentation currency	Total assets (EUR mio)	Total equity (EUR mio)	Revenue 2020 (EUR mio)	Revenue 2019 (EUR mio)
1	American Airlines Group Inc.	US GAAP	USD	€56.405	€3.543	€15.179	€40.833
2	Delta Air Lines Inc.	US GAAP	USD	€58.672	€1.250	€14.967	€41.989
3	Deutsche Lufthansa AG	IFRS-EU	EUR	€39.484	€1.387	€13.589	€36.424
4	United Airlines Holding Inc.	US GAAP	USD	€48.505	€4.831	€13.443	€38.641
5	Air-France-KLM S.A.	IFRS-EU	EUR	€30.211	€ (5.418)	€11.088	€27.188
6	China Southern Airlines Ltd.	IFRS-IASB	RMB	€40.683	€10.612	€11.754	€19.951
7	Air China Ltd.	IFRS-IASB	RMB	€32.944	€10.442	€8.826	€17.605
8	International Consolidated Airlines Group SA	IFRS-IASB	EUR	€30.264	€1.316	€7.806	€25.506
9	Southwest Airlines Co.	US GAAP	USD	€28.187	€7.233	€7.922	€20.034
10	China Eastern Airlines Corporation Ltd.	IFRS-IASB	RMB	€35.481	€7.374	€7.458	€15.640
11	Turk Hava Yollari AO	IFRS-IASB	USD	€20.805	€4.387	€5.896	€11.817
12	Air Canada	IFRS-IASB	CAD	€18.495	€1.097	€3.812	€12.878
13	LATAM Airlines Group SA	IFRS-IASB	USD	€12.754	€ (1.990)	€3.435	€8.995
14	Alaska Air Group Inc.	US GAAP	USD	€11.446	€2.435	€3.122	€7.844
15	JetBlue Airways Corp.	US GAAP	USD	€10.295	€3.220	€2.589	€7.230
16	SAS AB	IFRS-EU	SEK	€5.724	€1.045	€1.956	€4.355
17	Sky West Inc.	US GAAP	USD	€5.613	€1.744	€1.862	€2.655
18	Spirit Airlines Inc.	US GAAP	USD	€6.845	€1.834	€1.585	€3.422
19	Aegean Airlines SA	IFRS-EU	EUR	€1.310	€78	€318	€1.309
20	Finnair Oyj	IFRS-EU	EUR	€3.465	€897	€829	€3.098
21	Hawaiian Holdings Inc.	US GAAP	USD	€3.242	€489	€740	€2.530
22	Air Arabia PJSC	IFRS-IASB	AED	€2.901	€1.033	€442	€92
23	Icelandair Group hf	IFRS-EU	USD	€843	€190	€380	€1.344
24	Jazeera Airways co	IFRS-IASB	KWD	€449	€33	€118	€305
				€505.652	**€59.062**	**€139.116**	**€351.735**

Exchange rate	Exchange rate 31 December 2020 (= 1 EUR)	average exchange rate 2020 (= 1 EUR)	average exchange rate 2019 (= 1 EUR)
ECB rates			
USD	1.2771	1.1422	1.1195
CAD	1.5633	1.5300	1.4855
RMB	8.0225	7.8747	7.7355
SEK	10.0343	10.4848	10.5891
Dutch Tax Authority rates			
AED	4.3620	4.1902	4.1190
KWD	0.3632	0.3474	0.3408

List of abbreviations:

AS	Auditing standards (US based);
ASC	Accounting Standards Codification;
CARES Act	Coronavirus Aid, Relief, and Economic Security Act;
COVID-19	Coronavirus disease of 2019;
EoM	Emphasis of matter;
ESMA	European Securities and Markets Authority;
FASB	Financial Accounting Standards Boards;
IAASB	International Auditing and Assurance Standards Board;
IAS	International Accounting Standards;
IATA	International Air Transport Association;
IFRS	International Financial Reporting Standards;
IFRS-EU	International Financial Reporting Standard – European Union;
IFRS-IASB	International Financial Reporting Standard – International Accounting Standards Board;
ISA	International Standards of Auditing (issued by IAASB);
KAM	Key audit matter;
MURG	Material uncertainty relating to going concern;
NBA	De Nederlandse Beroepsorganisatie van Accountants (Dutch association for auditors);
PCAOB	Public Company Accounting Oversight Board;
SEC	Securities and Exchange Commission; and
US GAAP	United States of America Generally Accepted Accounting Principles.