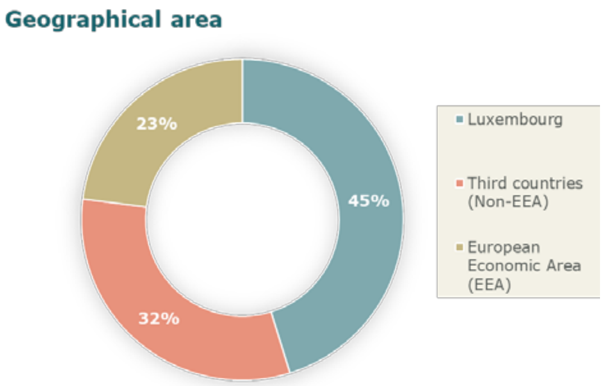
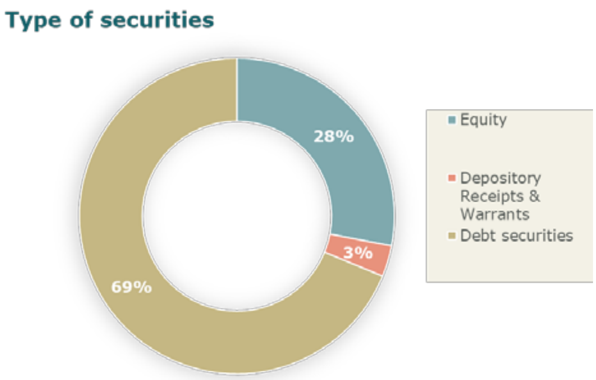
RESULTS OF THE ENFORCEMENT OF THE 2020 FINANCIAL AND NON-FINANCIAL INFORMATION PUBLISHED BY ISSUERS SUBJECT TO THE TRANSPARENCY LAW

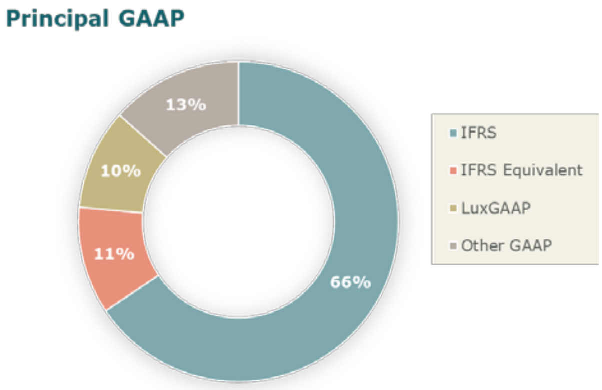
1. Introduction

The CSSF is the competent authority to ensure the supervision of securities markets. In this context, the CSSF is in charge of examining that the financial and non-financial information, published by issuers under its supervision, is drawn up in accordance with the relevant reporting framework, thereby contributing to investors' protection and promotion of confidence in financial markets.

Population of issuers falling within the scope of financial information enforcement as at 1 January 2021







2. Enforcement activities carried out in 2021

The selection of the issuers that are examined each year is based on a mixed model in which a risk-based approach is combined with a sampling and a rotation approach. The risk-based approach adopted considers the risk of a misstatement as well as the possible impact of such a misstatement on the financial markets.

2021 priorities

In its communiqué dated 9 December 2020, the CSSF presented the priorities for its 2021 enforcement campaign, mainly based on European common enforcement priorities (“ECEPs”) and with a strong focus on the need to provide adequate transparency regarding the consequences of the Covid-19 pandemic. They can be summarised as follows:

- Priorities related to IFRS financial statements
  - IAS 1 *Presentation of Financial Statements*
  - IAS 36 *Impairment of Assets*
  - IFRS 9 *Financial Instruments* and IFRS 7 *Financial Instruments: Disclosures*
  - IFRS 16 *Leases*
- Priorities related to non-financial statements
  - Impact of the Covid-19 pandemic on non-financial matters
  - Social and employee matters
  - Business model and value creation
  - Risk relating to climate change

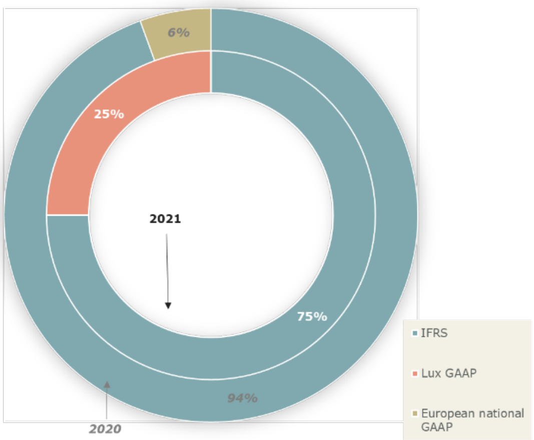
On top of these priorities and in line with its previous thematic reviews on issuers’ non-financial information, the CSSF has performed a thematic review on the current and historical non-financial reporting practices, focused on climate and environmental matters. Details and results on this thematic review are available in the CSSF’s report dated 29 November 2021.

2021 campaign

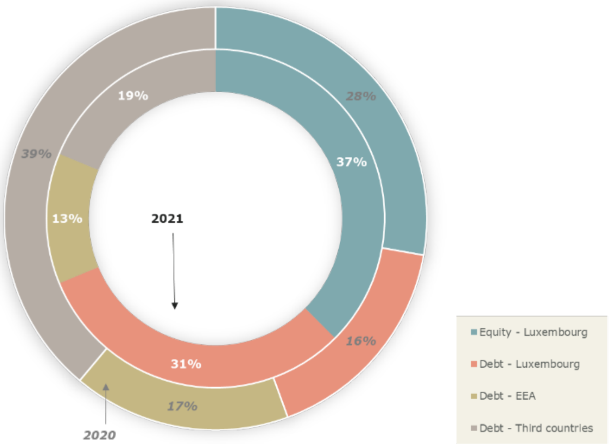
As part of the examination process and depending of the topics covered, the CSSF identifies the most effective way for examining the selected financial and non-financial information. The enforcement activities performed in 2021 then consisted of a combination of thematic, focused and unlimited examinations.

Thus, the examinations (excluding the thematic review of non-financial information) performed in 2021 covered 17% (2020: 21%) of the issuers falling within the scope of enforcement of financial information and can be further illustrated on the basis of the following criteria:

Examinations by accounting standards used by issuers in 2021 and 2020



Examinations by type of securities admitted and country in 2021 and 2020



3. Main findings on 2021 priorities related to financial information

IAS 36

In 2021, the CSSF carried out focused examinations on the application of IAS 36 on tangible and intangible assets for a selection of issuers. The issuers selected were those whose businesses were potentially most impacted by the Covid-19 pandemic, and who had assets on their balance sheet that were likely to be impaired.

We have noted that the majority of these issuers have fairly assessed the recoverable amounts of cash-generating units. They have also provided adequate disclosures on how management has updated its assumptions to reflect the latest available information and how such assumptions and measurements have changed compared to the last reporting period.

Thus, most of the issuers reviewed have revised their forecasts as from 2020 onwards and, where necessary, have already recognised impairments on their goodwill in the first half of 2020.

Budgets, used for the impairment tests, appear to have taken into account reasonable, even conservative, forecasts to capture any risk of impairment immediately. Indeed, activity recovered faster than expected after the first lockdowns in the first semester of 2020, although it did not immediately reach pre-Covid-19 levels. Thus, for most of the issuers under review, results were better than forecasted for 2020, and budgets met or exceeded. Whereas the use of multiple scenarios is encouraged in order to better assess the recoverable values despite the uncertainties related to the COVID-19 pandemic, we have noted that only few of the issuers reviewed have used this approach when determining the recoverable amount of their CGUs.

The robustness of the projections also supports that, while all issuers also provided the required sensitivity analysis for significant changes in key assumptions, they did not modify the range of sensitivities for these assumptions, as the uncertainty was already factored in the projections.

In addition to these two main factors, issuers have also taken steps to maintain their cash flow at satisfactory levels, notably by resizing their activities and postponing certain investments in order to have sufficient resources to cope with the decrease in their revenues.

Looking ahead, a critical disclosure provided by all issuers examined is the time horizon considered in relation to returning back to pre-Covid-19 cash flow or normal activity. Such horizon may vary between industries, ranging from ‘in the course of 2021’ to 5 years.

The continuous effect of the pandemic in 2021 due to the multiple variants and the resulting political measures will remain a challenge for issuers in their forecasting exercise for the coming years.

Application of IFRS 9 and IFRS 7

As planned, the CSSF analysed, through a thematic review, the disclosures provided by a selection of corporates and credit institutions on risks arising from financial instruments and expected credit losses (ECL) in the context of the Covid-19 pandemic.

Corporates

We noted that, although all issuers reviewed disclosed information on how financial risks arise and how they are managed (especially for liquidity risk), narrative explanations on financial risk concentrations could still be enhanced. We were satisfied to note that most issuers consider reasonable and supportable information, including available forward-looking information, when assessing impairment.

We expected issuers that recognise material amounts of trade receivables to disclose more specific information on potential impacts of the uncertainties related to the health crisis in the measurement of ECL. In that respect, we noted that almost half of the issuers reviewed did not provide any information on whether they had incorporated the effects of the Covid-19 crisis in their ECL model estimates, thereby hindering an informed understanding of their situation. However, we also observed examples of good disclosure from issuers explaining how they updated their credit risk management practices, e.g. by applying a premium on the ECL for customers in sectors most affected by the pandemic.

Credit institutions

All issuers included in our sample disclosed that they made changes in the estimation techniques or significant assumptions due to the Covid-19 crisis. However, the quality of the explanations provided in this respect has been found uneven, notably in the description of the different macro-economic scenarios used in the projections and of the management overlays.

On this topic, we also refer to the ESMA report on the application of the IFRS 7 and IFRS 9 requirements regarding banks' ECL (ESMA32-339-169).

IFRS 16

As part of our focus on the consequences of the Covid-19 pandemic and following our previous findings on the application of IFRS 16 in the 2019 financial statements, highlighting weaknesses in presentation and disclosure, we have reviewed a selection of financial statements of issuers where the application of IFRS 16 has a material impact.

Issuers concerned were either lessee or lessor, or both.

Firstly, the application of the practical expedient in paragraph 46A of IFRS 16 (Covid-19 related rent concessions) did not have a material impact on the financial statements of the lessees reviewed.

Among the lessors concerned, all issuers disclosed qualitative information on rent concessions granted under Covid-19, often also including quantitative information (impact on ECL). Overall, we found clear disclosures on the accounting policy applied regarding the relief measures granted. One issuer rightfully performed a sensitivity analysis on LGD (loss given default) rate changes applied on finance lease receivables.

Generally, the information provided by issuers to understand the impact of Covid-19 on their financial position, performance and cash flows has been considered adequate.

Indeed, the pandemic has changed the assumptions used by the issuers in the subsequent measurement of their right-of-use asset. In addition, some extension options have been exercised specifically due to the circumstances created by these new market conditions.

We also examined the general presentation and disclosures in relation to leases for lessees, which showed a substantial improvement compared to last year:

- All issuers disclosed adequate information required by paragraphs 53 & 58 of IFRS 16 (i.e. amounts to be presented for the reporting period by the lessee), including a separate maturity analysis of their lease liabilities; and
- When relevant, issuers disclosed additional qualitative and quantitative information about their leasing activities, notably regarding their exposure arising from variable lease payments and extension options and termination options.

4. Main findings on priorities related to non-financial information

Social and employee matters

We observed that all issuers under review provided information in relation to the issues of inclusion and diversity to the extent necessary for an understanding of the development, performance, position and impact of their activity. Moreover, regarding Covid-19 impacts, transparency on employee-related matters was provided, especially about health and safety.

Some areas for improvement were however identified. Few issuers disclosed information about targets established in the context of Covid-19 pandemic (e.g. forecast date for a safe return of employees on-site) and/or about whether new policies put in place (e.g. right to work remotely) were permanent.

Business model and value creation

We noted that globally, issuers provided a description of their business model, including information about its functioning and its expected future development, allowing readers to get an understanding of its implications for the non-financial matters. Nevertheless, we did not find in the sample reviewed any formal definition of value creation, as was encouraged by ESMA.

However, we would have expected and appreciated better disclosure of the Covid-19 impacts on the issuers' business model and policies in place.

Risk relating to climate change

While issuers under review generally addressed some climate change-related matters in their non-financial statements, the quality of the disclosure was uneven. Notably, several issuers failed to disclose both physical and transitional risks related to climate change and to describe the processes for managing these risks.

Moreover, issuers often did not disclose whether they consider in their planning process how risks and opportunities connected to climate change may evolve, nor did they include different time horizons in their risk disclosures.

We refer to our thematic review performed on issuers' climate and environmental related disclosures for more information about this topic.

5. Results of the unlimited examinations of financial information

In addition to the focused and thematic examinations discussed above, unlimited examinations have also been carried out during the 2021 enforcement campaign. Unlimited examinations consist of the evaluation of the entire content of the financial information included in one or more harmonised documents of an issuer in order to identify areas that, in the enforcer's opinion, need further analysis, and the subsequent assessment of whether the financial information regarding those areas is in accordance with the relevant financial reporting framework. An unlimited examination usually entails an interaction between the enforcer and the issuer. Based on the examination procedures undertaken and the information received from the issuer, the enforcer then concludes whether infringements exist in relation to the areas analysed.

The unlimited examinations carried out in 2021 covered 10% of the total population of issuers under our supervision and resulted in the vast majority of the decisions taken. In this context, the actions vis-à-vis certain issuers aim to either correct the identified errors or amend and improve the subsequent published financial statements.

Presentation in financial statements

A significant part of the decisions taken in the context of the 2021 unlimited examinations was in relation to the application of the presentation standards such as IAS 1 or IAS 34 *Interim financial reporting*. Even if these standards have been adopted for a long period of time and are well-known by the preparers of the financial statements, we continue to identify issues which could be easily avoided. Indeed, it is notably the case for the requirement of paragraph 20 of IAS 34 regarding the comparative statements (in particular for the statements of cash-flows and changes in equity) which are frequently misstated as well as for the requirement of paragraph 103 of IAS 1 regarding the cross-reference in the statement of cash-flows. In the context of the pandemic, comparatives and cross-references are of particular interest to the user of the financial statements in order to better understand the Company's activity in non-standard circumstances.

Following paragraph 20 of IAS 34:

Interim reports shall include interim financial statements (condensed or complete) for periods as follows:

[...]

(c) statement of changes in equity cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year.

(d) statement of cash flows cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year.

Alternative Performance Measures (APMs)

Furthermore, misstatements continue to be identified in relation to the application of ESMA Guidelines on Alternative Performance Measures, even though these Guidelines are applicable for more than five years. For instance, explanations on the use of APMs or numerical reconciliations are still often missing or misstated. The CSSF reminds that providing the definition of an APM is not sufficient for explaining the use of the measures presented.

> **Extract of ESMA Guidelines on Alternative Performance Measures (ESMA/2015/1415)**
>
> *Explanation on the use of APMs*
>
> 33. Issuers or persons responsible for the prospectus should explain the use of APMs in order to allow users to understand their relevance and reliability.
>
> 34. Issuers or persons responsible for the prospectus should explain why they believe that an APM provides useful information regarding the financial position, cash-flows or financial performance as well as the purposes for which the specific APM is used.

Fair value measurement

During our examinations, we noticed many weaknesses when examining the fair value measurement, notably for investment properties (IAS 40 *Investment Property* and IFRS 13 *Fair Value Measurement*). Issues identified in the review of issuers' fair value measurements included the disclosure of incorrect assumptions and the lack of information about fair value measurements classified in Level 3 of the fair value hierarchy. This information is however useful to the user of the financial statements as those measurements have a greater degree of uncertainty and subjectivity. In this context, we would like to recall the importance of disclosing the information requested by paragraph 94 of IFRS 13.

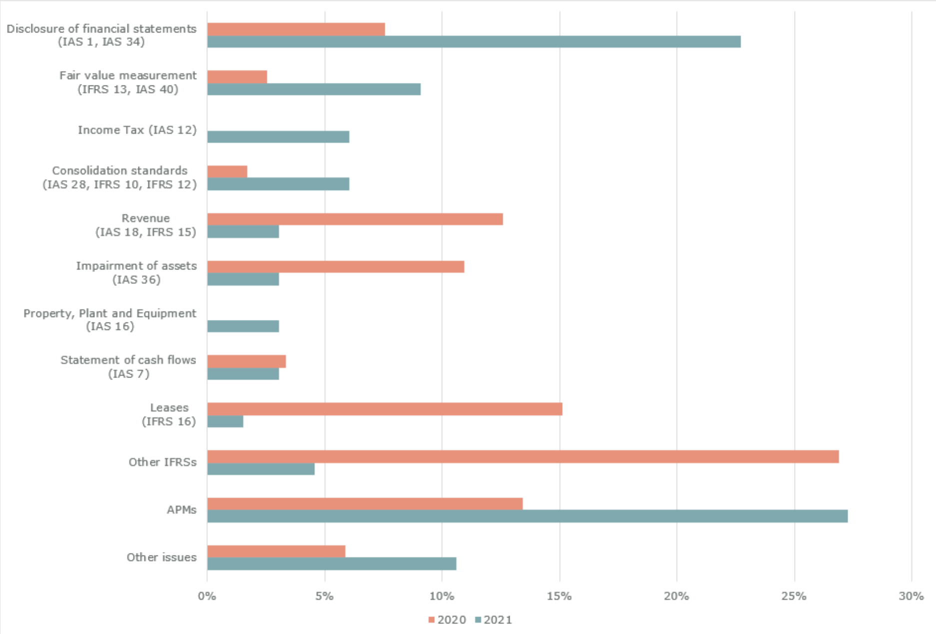
> **Following paragraph 94 of IFRS 13**
>
> "An entity shall determine appropriate classes of assets and liabilities on the basis of the following:
>
> (a) the nature, characteristics and risks of the asset or liability; and
>
> (b) the level of the fair value hierarchy within which the fair value measurement is categorised.
>
> The number of classes may need to be greater for fair value measurements categorised within Level 3 of the fair value hierarchy because those measurements have a greater degree of uncertainty and subjectivity. Determining appropriate classes of assets and liabilities for which disclosures about fair value measurements should be provided requires judgement. A class of assets and liabilities will often require greater disaggregation than the line items presented in the statement of financial position.
>
> However, an entity shall provide information sufficient to permit reconciliation to the line items presented in the statement of financial position …

Other subjects

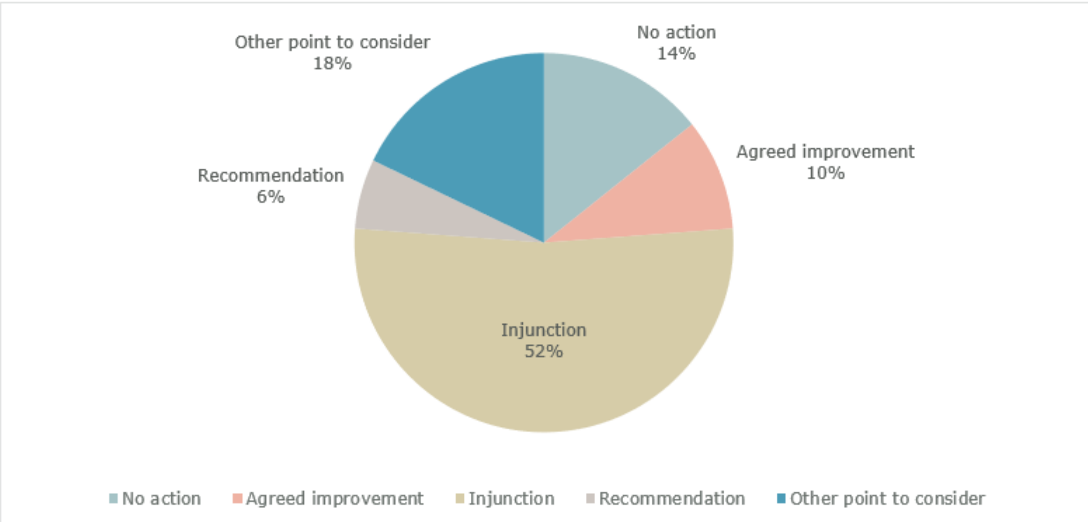
Outside of the area of IFRS, several actions were taken in the context of Luxembourg legal and regulatory requirements (Lux GAAP) in particular with regard to the amortisation of formation expenses as well as with respect to the content of the management report, where information and amounts presented were misstated or did not match with the financial statements.

6. Quantitative data on the decisions taken by the CSSF during its 2021 Enforcement campaign

Breakdown by topic of notifications



Breakdown by type of decision



Amongst the decisions taken in the course of the examinations performed by the CSSF, 52% of the total decisions were injunctions pronounced as the accounting treatment or the presentation was not in conformity with the applicable reporting framework or missing disclosures had been noted. 10% represented agreed improvements with issuers on the accounting treatment or disclosures to be made. Another 6% of decisions represented recommendations to improve the financial information in the future financial statements.

The other point to consider mainly relates to the examination of the non-financial reporting. In this regard, we have sent our observations to the issuers in advance before making any formal decisions. These observations have led to constructive discussions with the preparers of the non-financial reporting with the aim of improving the completeness, quality and reliability of the information given in these reports.

Lastly, we also investigated several issues or areas where we concluded that the reporting framework has been duly respected and no further action was deemed necessary, after exchanges with the issuers concerned.

7. ESEF

The CSSF reminds issuers that, they shall prepare their annual financial statements (AFRs) as from the financial year 2021 in compliance with ESEF.

Therefore, issuers should publish their AFRs in XHTML, a human readable standard which can be opened with any standard web browser. Where AFRs include IFRS consolidated financial statements, issuers shall mark-up those consolidated financial statements using XBRL tags, which make the labelled disclosures structured and machine-readable.

For further detailed assistance, issuers can consult the dedicated page on ESMA's website.

8. Outlook / Next steps

Even if the economic environment has been uncertain in 2021, globally the activity of most of the issuers under the supervision of the CSSF has recovered quickly after the downturn in 2020.

Currently, the consequences of the Covid-19 pandemic and of the Ukraine crisis could impact some sectors in unpredictable ways, slow down the level of activity sharply and deeply affect the results and the forecasts of the issuers. Depending on whether or not they existed at the end of the reporting period, these uncertainties should be considered carefully when preparing financial reports. In this context, issuers should continue to estimate and present their effects on their main KPIs, how they mitigate the related risks and how they address these main uncertainties.

On 17 December 2021, the CSSF has released its priorities in relation to the enforcement of the 2021 financial information published by issuers subject to the Transparency Law. As highlighted in this communication, the CSSF will monitor amongst others the ECEP for the 2021 financial reports.

Further information on ESMA's ECEPs can be found on the CSSF website under Enforcement of financial information.

2021 publications

During the year 2021, the CSSF has issued several publications and relayed relevant communications from ESMA. They can be found on the CSSF website:

https://www.cssf.lu/en/enforcement-of-financial-information

Date	Document		Link
17.12.2021	Communiqué	Enforcement of the 2021 annual reports published by issuers subject to the Transparency Law	Link
29.11.2021	Communiqué	Issuers: Phased-in implementation of Article 8 of the EU Taxonomy Regulation as from 1 January 2022	Link
29.11.2021	Studies and reports	Thematic review on Issuers' climate & environmental related disclosures	Link
22.02.2021	Communiqué	Results of the enforcement of the 2019 financial information published by issuers subject to the Transparency Law	Link
12.02.2021	Annual statistics	Population concerned by the enforcement	Link
20.01.2021	Press release	Delay by one year of ESEF requirements for listed companies	Link