EY Center for Board Matters

COVID-19: Board oversight of corporate finance in uncertain times

Building a better working world

There are any number of board responsibilities around the governance of corporate finance matters, including appropriate capitalization, forecasting cash flows, and use of short- and long-term debt financing. During times of uncertainty, the board plays a key role by providing strategic insight, oversight and foresight around whether the company's financial scenario planning and stress testing are designed to adequately assess the levels of liquidity, credit and capital needed over relevant ranges, as well as to confirm that appropriate communications are occurring with all stakeholders. By leveraging their collective experience and business judgment, directors can ask probing questions and provide appropriate guidance that will assist management through times of uncertainty, business disruption and financial instability. Boards can significantly assist management in how they respond to the crisis — starting with assessing the situation and stabilizing the business.

When it comes to forecasting, scenario planning and stress testing, boards should challenge management to focus not only on short-term forecasts but also mid- and long-term planning horizons. Above and beyond reviewing the standard best-, worst- and most-likely case scenarios, there is a need to understand immediate and future demand and supply shocks, as well as the impacts of potential stimulus packages. Robust, scenario-enabled modeling allows for more fact-based decision-making. Boards should consider asking:

- What key drivers and levers in forecast models are being focused on to understand and counteract the downward momentum?
- What are the key risk scenarios, and how is probabilistic forecasting being used to assess market, economic and financial impacts of disruptive events and corresponding shifts in business trajectories?
- Which business units/assets are affected immediately vs. in the mid- to long-term?
- Under what scenarios does the company hit key breakpoints related to covenant noncompliance, credit squeeze and access to existing capital sources?
- Does the forecast factor in claims for negative events under contracts, government programs and insurance policies?
- As management receives new data, what is the cadence and method for communicating with the board around new scenario and sensitivity analyses?

In its oversight of the financial sustainability of the organization, one of the board's most important goals is understanding how adequate financial reserves and liquidity are assessed and maintained. Armed with the insights from robust scenario planning and stress testing, the board should assess the level of liquidity and access to capital with questions such as:

- Have all options been explored to extend the company's liquidity runway, including one-time revenue opportunities, cost reduction, working capital crisis management techniques, idling cash-burning operations, and deferring capital expenditures and/or research and development?
- Have existing financing agreements been reviewed to determine flexibility with upcoming principal and interest payments?
- Given the existing capital structure, are there immediate needs for additional short-term liquidity?
- Has the company created adequate headroom for unanticipated cash needs, including abrupt sales declines and distressed suppliers?

- Does the company's scenario planning and stress testing allow company management to take control and establish credibility and clearly articulate both the current situation and the expected outcomes to all stakeholders?

As the credit markets, economy and global supply chains begin to stabilize, boards will need to provide the foresight to help management navigate the potential paths forward. Scenario option modeling as companies emerge from the crisis is also important but often overlooked. This may involve not only a recovery, but perhaps a business strategy that is completely reimagined. Some considerations include:

- How is the company reevaluating capital allocation strategies and revisiting key investments to drive total stakeholder value under various recovery scenarios?
- Are there tax plans that should be implemented to take advantage of potentially reduced values?
- Are there scenarios under which opportunistic acquisitions, buyouts of business partners, dividends or stock buybacks are considered, given lower valuations and the company's cash position?
- Is this an opportunity to assess alternatives to take the business private and recapitalize?
- How does the company better fulfill its purpose and drive long-term value for all stakeholders using lessons learned? What great results are possible to achieve going forward?

During times of great uncertainty, such as the current COVID-19 pandemic, boards play a critical role in assisting management through business disruption and financial instability. Asking the right questions, at the right time, not only helps companies assess and stabilize the organization. It also allows them to recover and, in some cases, reimagine the business entirely.

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