



Will COVID-19 Affect/Infect Your Audit (and financial reporting)?

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Topics

- Accounting for various economic stimulus programs
- Internal controls & working remotely
- Remote auditing
- Subsequent event disclosures
- Risks and uncertainties disclosures
- Going concern considerations
- Asset impairment
- Cash flows



Accounting for Stimulus programs

- Payroll Protection Program (PPP):
- Record as a LOAN:
 - It is not a contribution until certain requirements are met
 - Record as a contribution when the bank approves forgiveness
 - You won't know the amount forgiven until then



Accounting for Stimulus programs

- Families First Coronavirus Relief Act-
FFCRA Credits:
- Wages credits from PR taxes for leave
 - Employer's gross income is increased
 - Record PR taxes at gross



Accounting for Stimulus Programs

- Employee retention credit:
- 50% of up to \$10K in wages and healthcare costs paid from 3/12/20-12/31/20 (not eligible if you have SBA loan)
 - Credit is taken against payroll taxes
 - Same as FFCRA credits: gross up the amounts



Accounting for Stimulus Programs

- Payroll tax payment deferral:
- Defer paying payroll taxes (employer's portion) through 12/31/20.
- Repay 50% on 12/31/21 and 50% on 12/31/22
 - Record payroll taxes expense at gross amounts as they are incurred
 - Record liability for the amount deferred
 - June 30 year-ends: 100% of the liability would be long term
 - December 31 year-ends: 50% of the liability would be long term



Poll question

When you receive the proceeds from your PPP loan, you should record it as:

- (1) A loan payable
- (2) A conditional contribution
- (3) An unconditional contribution
- (4) Miscellaneous income



Internal controls

- Auditor is required to:
 - Obtain an understanding of controls that are relevant to the audit
 - Assess whether controls are designed effectively to prevent or detect/correct material misstatements
 - Determine whether controls have been implemented
 - Identify where and how the financial statements may possibly carry a higher risk of misstatement
 - Design audit procedures to address these risks



Internal controls

- Understanding of internal controls must first be obtained before determining whether performing audit procedures remotely would be effective
- There could be 2 different systems to understand: pre-March 15, 2020 and post-March 15, 2020
 - Accounting process memos will need to cover both time frames
- Consider:
 - How were transactions processed?
 - What controls were in place?
 - What was the level of business activity during that time?



Internal controls

- Questions the auditor may ask:
 - What was the message from the CEO/Board?
 - What was the message from the CFO/Controller to the Accounting Department?
 - Was there any training or guidelines provided for working remotely?
 - How did approval processes change?
 - How involved were top management in transaction processing/approvals?
 - How did communication work across the accounting department?
 - What controls dropped off during this time period?
 - Where did the opportunity for fraud open?



Working remotely

The best way to find out if you can trust someone is to trust them.

Ernest Hemingway



Working remotely – General

- Establish regular check-in meetings with your team
- Establish employee responsibilities to communicate
- Management remains accessible to employees
- Provide necessary training and coaching to employees
- Ensure technology is working and explore new ways to use it; What's next?
- Establish new policies or procedures



Working Remotely – Internal Controls- Cash Disbursements & Expenses

Example using manual system:

- Purchase orders – *Online form, email to approver, receive emailed approval, create online file on organization's server with the P.O.'s and approvals*
- Invoices – *From office, scan invoices and email to the processor and the approver*
- Matching – *Processor matches the P.O. to the invoice and emails to the approver who emails back approval which is stored in the online file*
- Accounts payable – *Processor prints to excel an A/P Aging from accounting software, highlights invoices to pay, and emails to check signer or approver, who emails back approval to pay those listed*



Working Remotely – Internal Controls- Cash Disbursements & Expenses

Example using manual system:

- Cutting checks – *Processor creates checks on a bi-weekly basis and leaves in the office for the check signer to sign and mail out; processor adds the approval and listing of checks from above to the online file*
- Signing checks – *Signer compares approved listing to the checks and reviews backup by reviewing scanned invoices, P.O.'s and approvals in the online file*
- Positive pay - *Processor creates Positive Pay report and sends to CFO who compares to check listings and approvals in the online file and then uploads the report to the bank.*



Working Remotely – Internal Controls- Cash Disbursements & Expenses

Other:

- Do not mail a vendor check to an alternative address
- Consider ACH payments (but stick with the same control process)
- Consider Bill.com- approvals are automated
- Expense reimbursements- same approval process, but forms and receipts can be emailed to the approver who approves and emails to processor
- Credit card charges- For CEO's charges, email credit card statement and copies of receipts to Board Treasurer for approval. Maintain approval in online file and instruct processor to not pay without it.
- Don't be a victim of fraud!
 - Email from someone posing as vendor asks you to change bank info for ACH payment to them.



Working Remotely – Internal Controls- Cash Receipts and Revenue

Example using manual system:

- Billings (fees revenue) – *Approvals of billings via email before they are submitted; maintain separate online file of approvals with billings attached.*
- Deposits – *From office, scan copies of checks with backup, create log of checks, and email to the processor, the CFO, and Development. Maintain in online file.*
- Donations - *Development enters into donor software and records restrictions.*
- Bank reconciliations – *Processor prepares, CFO reviews and approves with approval maintained in the online file. CFO compares deposits recorded in accounting software to daily cash receipts logs and donor software.*



Working Remotely – Internal Controls- Cash Receipts and Revenue

Other:

- Send a notice to (or otherwise encourage) donors and payer sources to pay electronically or to use your website for payment
- Set up a lock box at your bank



Working Remotely – Internal Controls- Payroll

Example using manual system:

- Timecards– *Approvals via email; timecards and approvals emailed to processor (copy CFO) and stored in online file*
- Processing– *Done online; pre-submittal payroll report to CFO for approval; maintain approval and report in online file*
- Issue checks - *Final payroll report emailed to CFO for approval. CFO compares to approved pre-submittal report. Final approval maintained in online file.*
- Payroll JE's– *CFO reviews and approves with approval maintained in the online file.*
- Don't be a victim of fraud!
 - Email from someone posing as an employee and asks you to change direct deposit bank account for their paycheck. Call individual to verify.



Working Remotely – Internal Controls- Overall Financial Reporting

- Maintain a set schedule of weekly financial reporting with management
 - A/P Aging
 - A/R Aging
 - Promises to give schedule
 - Cash journal (showing disbursements and deposits)
- Maintain a set schedule of monthly financial reporting with the Finance Committee and Board of Directors
 - Budget to actual report
 - Cash flow projection
 - Income statement and balance sheet
 - Other (dashboard, etc.)
- Assign responsibility for ensuring these schedules are met and for follow up



Cash flow

- Understand your cash flow to help with decision making- prepare a cash flow projection:
 - Estimate of cash inflows and outflows by week or month
 - When will cash flow become a problem?
 - What can be done now to prevent it?
 - Keep the projection updated
- Different from a budget



Cash flow

- Options to consider with cash flow projection info:
 - Can you speed up collection of receivables/promises?
 - Offer e-payment options
 - Manage collections closely
 - Will a funding source provide an advance?
 - Can debt be refinanced for a lower monthly payment?
 - Can donors be asked to release restrictions?
 - For cancelled events, can the entity ask those attendees to convert their payment to a donation?
 - Can expenses be cut or projects deferred?
 - Categorize as “must”, “should”, and “nice to”
 - Can payment of payables be slowed?
 - Pay timely but not early
 - Consider staffing levels



Cash Flow

- Options to consider with cash flow projection info (continued):
 - With all of the previous considered, determined, and incorporated into the projection, when does cash flow become a problem? How much?
 - Line of credit increase?
 - Access to a reserve/savings?
 - Nonprofit Finance Fund- cash flow tool



Poll question

Internal controls in the accounting process system can be maintained, even when working remotely

- (1) True
- (2) False



Auditing remotely

- Questions on internal controls may need to be asked in a virtual group meeting
- Challenge for auditors in ensuring controls have been implemented
 - May also be done virtually
 - Consider differences with employees working from home
 - Inquiry alone is not sufficient



Auditing remotely

- There may be increased or new risks of material misstatements
- If there are risks...
 - Has the organization considered this due to the changes?
 - Have mitigating controls been put in place to address the risks?
 - Has the Finance Committee or Board been involved in the process/discussion?



Auditing remotely

- Increased # of significant deficiencies or material weaknesses?
 - SD: Merits the attention of those charged with governance
 - MD: Reasonable possibility that a material financial statement misstatement will not be prevented or detected/corrected on a timely basis



Auditing remotely

- Inventory observations
 - *Can auditors use cameras and other technologies to observe inventory if they are unable to attend in person?*
 - Yes. Auditors need to ensure comfort level with video being at appropriate location.



Subsequent events

- Required to be disclosed
- 2 types:
 - Events/transactions that provide additional evidence about conditions that existed at year-end
 - Events that provide evidence about conditions that did not exist at year-end
- For 12/31/19 year-ends, the pandemic is a Type II subsequent event
 - Disclosure required
 - No adjustment to financial statements
 - Describe nature of the event and if possible, estimate effect on financial statements



Subsequent events

Considerations:

- Less demand results in loss of revenue
 - Entities that operate with groups of people: arts/cultural, healthcare services, shelters or special schools for children, etc.
 - Operations closed
- More demand for services, but no increased revenue
- Loss of donations or contract revenue
- Decreased cash flows
- Line of credit
- Not able to meet debt covenants
- Modification of debt terms
- Special event cancelled



Subsequent events

- Stock market declines
 - *If there is a significant decline in investment market value after year-end, should the balance be adjusted at year-end?*
 - Required to recognize the effects of all subsequent events that provide additional evidence about conditions that existed at the year-end date, including estimates
 - Do not recognize subsequent events that provide evidence about conditions that did NOT exist at the year-end date, but arose after (but before issuance)
 - Answer: Do not adjust year-end balance for changes in fair value, but consider disclosure



Subsequent events

- What about June 30, 2020 year-ends?
- For 6/30/20 year-ends, there may need to be more disclosure as effects become known
 - Consider adjustments to financial statements (e.g., allowance, bad debt)
 - Inventory write downs
 - Consider additional disclosures



Poll question

An organization should consider disclosing which of the following in their financial statements related to subsequent events:

- (1) Loss of a substantial contract after year-end
- (2) Had to close operations due to pandemic
- (3) Unable to meet debt covenant requirement one month after year-end
- (4) All of the above



Risks and Uncertainties

- Disclosures required that focus primarily on risks and uncertainties that could significantly affect the amounts reported in the financial statements in the near term.
Can stem from:
 - Nature of operations
 - Use of significant estimates
 - Current vulnerabilities due to certain concentrations



Risks and Uncertainties

- Significant estimates
 - When info is known before the financial statements are issued → Disclosure if:
 - It's at least reasonably possible that the estimate will change in the near term due
 - The effect of the change would be material

Examples: A/R Allowance, Inventory Allowance, Investments



Risks and Uncertainties

- Current vulnerabilities- Concentrations
 - Exposed to risk of loss
 - When info is known before the financial statements are issued → Disclosure if:
 - It's at least reasonably possible that the concentration would cause near-term severe impact



Risks and Uncertainties

- Current vulnerabilities- Concentrations
 - Examples:
 - Concentration in volume of business with a funding source, supplier, lender, grantor, or contributor
 - Concentration in revenue from particular services or fund-raising events
 - Concentration in available sources of materials, labor or services
 - Concentration in the market or geographic area



Going concern

- Management has the responsibility to assess whether there are conditions or events that raise substantial doubt about the entity's ability to continue operations within 1 year after issuance
- Substantial doubt: conditions and events indicate that it is probable that the entity will be unable to meet its obligations as they become due within the next year.
 - Not meeting debt covenants
 - Debt coming due w/in 1 year
 - Significant loss of revenue (consider financial health of funding sources)
 - Significant investment losses
 - Maxing out line of credit to make ends meet
 - Using endowment funds above spending policy %
 - Inadequate funds to cover restricted donations
 - Negative net assets, losses, low current ratio



Going concern

- If there is a substantial doubt (whether or not you expect the doubt to be alleviated), requirement to disclose in footnotes
 - Management's plans
- If the doubt is *not* alleviated
 - Additional disclosure and “emphasis of matter” in auditor's report



Going concern

- *What if management is struggling with some of the assumptions and forecasts related to going concern given the volatility of our current environment?*
 - Management's plans to continue operations are always going to be a best estimate
 - Auditors are required to consider the reasonableness of being able to implement



Poll question

Which of the following may be required to be included as a disclosure in the footnotes to your audited financial statements?

- (1) Subsequent events
- (2) Risks and uncertainties
- (3) Going concern issues
- (4) All of the above



Asset impairment

- Property & Equipment:
 - Is there an event or circumstance that indicates that the carrying amount of the asset may not be recoverable?
 - Is the fair value less and not recoverable?
 - May need to write down to fair value
 - Held-for-sale assets should be written down to fair value at the time listed for sale