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Audit Planning Considerations as COVID-19 Pandemic Continues

As auditors begin to plan for 2021 year-end audits in year two of the pandemic, and global economic and health issues continue to evolve, there are numerous factors to consider when planning and performing your audit and identifying risks that could result in financial statement misstatements.

Planning

The following should be considered by auditors when planning their engagements:

Timing and Scope. Overall planning procedures should consider both auditor and client resources and changes to audit plans required because businesses continue to be shut down and people continue to work remotely. The timing and scope of the audit may have to change. Access to management, personnel, and client records may be limited.

Internal Controls. There may have been changes in internal controls and processes because of remote working and/or reductions in staff. Changes in internal controls (entity-level and activity-level) may make testing of controls difficult or impossible, and a substantive approach to the audit may be required. Reduced segregation of duties can cause control breakdowns and greater potential for management override and fraud. It may not be possible to meet with clients face-to-face, and video conferencing may have to be used for meetings and fraud inquiries.

Acceptance and Continuance. Client acceptance and continuance procedures should consider any changes in the client's organization, business operations, financial results, financing, and plans. Risk assessment procedures should consider new opportunities or incentives for fraud. Risk areas that may be greater due to the pandemic include accounting estimates, compliance with laws and regulations, going concern uncertainties, and subsequent events.

Audit Team. Audit team changes may be necessary, including the use of more experienced auditors and partners,

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consultations within the firm, and specialists to address new and more complex issues.

Materiality. Materiality levels may change based on changes in the company's business or the needs of users of its financial statements.

Analytical Procedures. Analytical procedures may not be sufficient because comparisons between the current and prior periods are not meaningful due to the pandemic's impact. This would apply to both preliminary and substantive analytics. It may be more difficult to develop expectations.

Financial Statements

The following are financial statement areas where COVID-19 may have greater audit implications:

Revenue Recognition. Revenue recognition issues related to changes in customer preferences, contract modifications, discounts and refund concessions, and changes in credit policies or payment terms should be considered. Related collectability of accounts receivable should also be considered.

Government Grants. New government grants may be accounted for as revenues or donor-restricted contributions. Government funding programs have eligibility, documentation, expense tracking, and other requirements for auditors to evaluate, and clients may be subject to government agency audits.

Estimates and Fair Values. Budgeting and forecasting of revenues, costs, and cash flows have implications for accounting estimates and fair values. Uncertain cash flows affect the discount rates used.

Investments. Investment fair values and financial instruments that qualified for hedge accounting can be negatively affected by market changes.

Inventory Values and Obsolescence. Supply chain disruptions and reductions in production can affect inventory quantities and values. Client physical inventory counts may be delayed or prevented because of travel and work restrictions. Auditor inventory observation may have to be done remotely or may be restricted. AU-C 501 requires alternative procedures if counting is not possible.

Property, Plant, and Equipment. Useful lives and related deprecation may change due to changes in business plans. There may also be potential impairment of long-lived assets and leased assets.

Goodwill and Intangible Assets. Goodwill and intangible assets may require impairment testing because of COVID-19 triggering events.

Accrued Liabilities. Accrued liabilities may be needed for employee terminations, changes in benefits, and payroll tax payment deferrals. Changes to contingency accruals should also be considered.

Long-term Debt. The compliance requirements of the Paycheck Protection Program (PPP) for loans and the probability of loan forgiveness should be considered. There may be debt classification issues for existing debt for failures to meet debt covenants. And there may be modification or debt extinguishment that occurred because of financial difficulties.

Deferred Tax Assets. Realizability because of current year losses, the impact on tax provisions, and the ability to estimate future events should be considered.

Reporting

In response to COVID-19, the AICPA issued SAS No. 141, *Amendment to the Effective Dates of SAS Nos. 134–140*, to delay the effective dates of SAS Nos. 134–140 for one year, until years ending on or after December 15, 2021. The new audit reports will need to be used for 2021 year end audit engagements.

Practical Consideration:

The CX-6.3 in all of the PPC audit titles provides an extensive list of risks associated with the COVID-19 pandemic that auditors need to consider as they plan and perform their audits. This practice aid has been tailored for the applicable industry title.

AICPA resources on COVID-19 are available at **https://future.aicpa.org/resources/toolkit/aicpa-coronavirus-resource-center**.

SEC resources related to COVID-19 can be found at **www.sec.gov/sec-coronavirus-covid-19-response**.

AICPA Issues Guidance on Accounting for Certain COVID-19 Relief Grants

In August, the AICPA issued Technical Q&A (TQA) 5270.01, *Recipient Accounting for Shuttered Venue Operators Grants and Restaurant Revitalization Fund Grants Received Under the Small Business Administration COVID-19 Relief Programs*.

The TQA provides guidance on which accounting models under existing GAAP to apply to these grants, and it applies to both for profit and not-for-profit entities. Publicly traded entities aren't eligible for either of these grants. Nonprofits aren't eligible for RRF grants.

These grants provide federal support to eligible entities that suffered revenue losses due to the COVID-19 pandemic. The funds were established by the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act and amended by the American Rescue Plan Act. The grants are administered by the Small Business Association's (SBA) Office of Disaster Assistance. Funds received may be used only for specific allowable expenses within dates specified in the grants and don't have to be repaid if used for eligible costs.

Shuttered Venue Operators Grants (SVOG)

SVOG will provide over $16 billion to businesses that suffered revenue losses due to closures because of restrictions on public gatherings as a result of COVID-19. The program began in April 2021, and applications for supplemental SVOG awards began in August. Applicants that qualify for initial SVOG grants may receive amounts equal to 45% of their gross earned revenue, up to $10 million.

Eligible entities include operators or promoters of live venues; theatrical producers; operators of live performing arts organizations, museums, and movie theatres; theatre owners; and talent representatives. These entities owned by state or local governments are eligible to apply if the government-owned entity solely acts as the venue operator and doesn't engage in other activities. The entity must have been in operation as of February 29, 2020.

Restaurant Revitalization Fund (RRF) Grants

RRF grants provided over $28 billion of emergency assistance for eligible restaurants, bars, and other businesses that serve food or drink that suffered revenue losses due to the pandemic. The program began in April 2021 and all the funds were used by the end of May, but legislative actions have been taken to consider adding additional funds.

Applicants that qualified for RRF grants received a minimum of $1,000 and a maximum of $5 million per location, or $10 million in total. The grants were calculated based on lost gross receipts from 2019 to 2020, or eligible expenses for businesses not in operation until 2020. If the grant isn't used in full by the end of the specified dates for the covered period, or if the business closes, the remaining funds must be returned.

Eligible entities include restaurants, snack bars, food trucks, bakeries, airport and sport venue concessions, bars and lounges, hotels and inns, wedding venues and caterer, breweries and wineries, and distilleries. To be eligible, certain entities must have onsite sales to the public of at least 33% of gross receipts. They may not own, or operate with affiliated businesses, more than 20 locations. Also, entities that received a SVOG or have a pending SVOG application aren't eligible.

Accounting for SVOG and RRF Grants

Business Entities. GAAP doesn't include explicit guidance for accounting for government grants by business entities. The TQA indicates FASB ASC 105, *Generally Accepted Accounting Principles,* provides the decision-making framework to use to determine which accounting guidance to apply when there is no specific GAAP guidance to apply—first analogize to other areas of authoritative generally accepted accounting principles before considering nonauthoritative sources. If grant amounts are material, entities should disclose in the notes to the financial statements the impact of the grants on the financial statements and their accounting policy for the grants.

International Accounting Standard (IAS) 20, *Accounting for Government Grants and Disclosure of Government Assistance,* FASB ASC 958-605, *Not-for Profit Entities—Revenue Recognition*, or FASB ASC 450-30, *Contingencies—Gain Contingencies*, are the principles the TQA suggests might be applied by analogy.

IAS 20 provides that a grant can't be recognized in income until there's reasonable assurance (it is probable)

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the recipient will comply with the grant's conditions and will receive the grant. The grant income is then recognized over the periods in which the related eligible expenses are recognized, with a liability recognized if grant payments received or receivable exceed the expenses incurred at the reporting date. Using IAS 20 guidance, the grant may be reported either as income or a reduction in the related expenses.

FASB ASC 450's model for recognizing gain contingencies calls for recognition when all contingencies for receiving the grant have been met and the gain is realized or realizable. Grant payments received would be recorded as a liability (refundable advance), which would be reversed at the time the grant proceeds are realized or realizable and recorded in income.

Not-for-Profit Entities. Government grants should be accounted for as contributions received under FASB ASC 958-605, *Not-for-Profit Entities—Revenue Recognition*. The TQA indicates because there are conditions to receiving the funds (having incurred eligible expenses) and keeping them (noncompliance with terms and conditions is grounds for returning the funds to the SBA), the grant payments are conditional and aren't recognized until the conditions are substantially met or explicitly waived by the government. Contribution revenue is recognized only to the extent eligible expenses were incurred. At each reporting date, grant payments received in excess of revenue that can be recognized would be recorded as a liability (refundable advance), which would be reversed and recorded in income at the time the eligible expenses are incurred in future periods.

Under FASB ASC 958-605, because the funds can only be used for eligible expenses, they are considered to be donor-restricted. But because those restrictions are likely satisfied at the same time as the conditions for receiving the funds, any revenue recognized would be reported as an increase in donor-restricted net assets with a reclassification to net assets without donor restrictions. If the entity elected the accounting policy option to "simultaneously release" donor-restricted contributions whose restrictions are met in the same reporting period, the contribution revenue can be reported directly in net assets without donor restrictions.

Practical Consideration:

Resources on the SVOG can be found on the AICPA's website at **https://future.aicpa.org/resources/article/understanding-the-shuttered-venue-operators-grant-program**. Resources on the RRF can be found on the AIPCA's website at **https://future.aicpa.org/resources/article/understanding-the-restaurant-revitalization-fund-rrf-grant-program**.