10 financial statement areas to watch for COVID-related effects

The COVID-19 pandemic is still adversely affecting many businesses and not-for-profit organizations, but the effects vary, depending on the nature of operations and geographic location. Has your organization factored the effects of the pandemic into its financial statements? You might not have considered this question since last year if your organization prepares statements that comply with U.S. Generally Accepted Accounting Principles only at year end.

As we head into audit season for 2021, it's time to evaluate whether your financial situation has gotten better — or worse — this year. Here are 10 financial statement areas to home in on:

1. Revenue recognition. Assess how changes in customer preferences, contract modifications, discounts, refund concessions, and changes in credit policies or payment terms impact the top line of the income statement. Also consider related collectability of accounts receivable.

2. Government grants. You may account for these grants as revenue or donor-restricted contributions. Government funding programs may have eligibility, documentation, expense tracking and other requirements (such as government audits) that you may need to address.

3. Estimates and fair values. These items are typically based on budgeting and forecasting of revenue, costs and cash flows. Uncertainty may *increase* the discount rates used in making estimates and *decrease* the fair values of certain balance sheet items.

4. Investments. Market changes caused by the pandemic may negatively affect the fair values of investments and financial instruments that qualify for hedge accounting.

5. Inventory. It's possible that certain market conditions — including inflation, reductions in production and supply chain disruptions — may affect the value of raw materials, work-in-progress and finished goods inventory. Consider the need for write-offs due to obsolescence.

In addition, travel and work restrictions may delay, restrict or prevent year-end physical inventory counts. Your external auditors may have to observe counts remotely, which, in turn, may require additional testing procedures during audit fieldwork.

6. Property, plant and equipment. Evaluate changes in useful lives and related deprecation due to changes in business plans. There may also be potential impairment of long-lived assets and leased assets.

7. Goodwill and other intangible assets. Because of COVID-19 triggering events, these items may require impairment testing and write-offs may be needed.

8. Deferred tax assets. Consider the realizability of these assets in light of current year losses and uncertainty about future events, including the impact of possible federal tax law changes.

9. Accrued liabilities. You may need to book additional liabilities this year for employee terminations, changes in benefits and payroll tax payment deferrals. Also consider whether existing contingency accruals are still adequate.

10. Long-term debt. You may have debt classification issues for existing loans if your organization fails to meet its debt covenants. Financial difficulties may result in debt modification or extinguishment. Also evaluate the compliance requirements of the Paycheck Protection Program (PPP) loans and the probability of forgiveness.

This list is a useful starting point for discussions about how the pandemic has affected financial results in 2021. If you have questions about how to report the effects, contact us for guidance. Your preparedness will help facilitate audit fieldwork and minimize adjustments to your in-house financial reports.