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FAQs — State and Local Government Financial Statement Accounting and Auditing Matters and Auditor Reporting Issues Related to COVID-19

Introduction

In our desire to serve AICPA members in the United States during this pandemic, and the public in general, the following representative frequently asked questions (FAQs) and topics have been compiled to aid (1) practitioners as they perform financial statement audit engagements of state and local governments in these uncertain times and (2) preparers of state and local government financial statements.

This document provides nonauthoritative guidance on accounting and auditing matters as developed by AICPA staff. Official AICPA positions are determined through certain specific committee procedures, due process, and extensive deliberation. The AICPA staff views expressed in this report are intended to provide member services, but not for the purposes of providing accounting services or practicing public accounting. The AICPA makes no warranties or representations concerning the accuracy of information issued.

GASB Resources

This AICPA document covers FAQs and topics related to the COVID-19 pandemic to assist both preparers of governmental entity financial statements and practitioners performing audits of those financial statements. However, auditors and preparers should be aware that GASB is also addressing the effect of the COVID-19 pandemic. As of the date of this publication, GASB had released for comment a proposed technical bulletin, *Accounting and Financial Reporting Issues Related to the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) of 2020 and Coronavirus Diseases*. The proposed technical bulletin includes various topics including clarification of the presentation of certain inflows of CARES Act resources and the unplanned and additional outflows of resources incurred in response to the COVID-19 pandemic. Look for the final technical bulletin, which is expected to be issued by July 2020, on GASB's website (www.gasb.org).

Additionally, GASB released an "[Emergency Toolbox](#)" to help stakeholders quickly identify GASB's authoritative guidance that could be relevant to the current circumstances. The toolbox also provides links to other professional organizations from which stakeholders may obtain nonauthoritative recommendations for financial reporting and other activities as governmental entities deal with the effects of the pandemic.

General Accounting, Auditing, and Reporting Matters

Subsequent Events

Financial Reporting Considerations Related to COVID-19 Pandemic

Governmental entities may need to evaluate whether the consequences of the COVID-19 pandemic represent subsequent events depending on the timing of their year-ends. Subsequent events are defined in GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*, as amended, as those events or transactions that occur subsequent to the statement of net position date but before the financial statements are issued. Some of those events and transactions (referred to as *recognized events*) require adjustments to the financial statements, and others (referred to as *nonrecognized events*) may require disclosure in the notes to the financial statements.

Recognized events are those that provide additional evidence with respect to conditions that existed at the date of the statement of net position and affect the estimates inherent in the process of preparing financial statements. Financial statements should be adjusted for any change in estimates as a result of evidence obtained subsequent to the date of the statement of net position.

Nonrecognized events are those that provide evidence with respect to conditions that did not exist at the date of the statement of net position but arose subsequent to that date. Those nonrecognized events may be of such a nature that their disclosure is essential to a user's understanding of the financial statements.

For fiscal years ending prior to the COVID-19 pandemic, any pandemic-related subsequent events identified would likely be nonrecognized subsequent events. Judgment is required and each entity will need to carefully evaluate its relevant facts and circumstances to determine the appropriate treatment for events related to the pandemic and determine whether the pandemic is viewed as a current period or a recognized or nonrecognized subsequent event based on the nature of the governmental entity and its financial reporting year-end.

GASB's proposed technical bulletin addresses another subsequent event consideration relating to what the appropriate treatment would be if amendments to the CARES Act are passed and signed into law after a government's statement of net position date but prior to the issuance of financial statements. Watch GASB's website (www.gasb.org) for the final technical bulletin. See also the earlier "GASB Resources" section for more information.

Fair Value Declines

Another common consideration is whether declines in the fair value of an asset subsequent to the date of the statement of net position should result in the adjustment of the financial statements given the recent stock market volatility. In contemplating this situation, consider the following guidance.

GASB Statement No. 56 paragraph 10, as amended, states that "events that provide evidence with respect to conditions that did not exist at the date of the statement of net position but arose

subsequent to that date...should not result in adjustment of the financial statements.” However, it also adds that some of these events “may be of such a nature that their disclosure is essential to the user’s understanding of the financial statements.”

GASB Statement No. 56 paragraph 12 indicates “changes in the quoted market prices of securities ordinarily should not result in adjustment of the financial statements because such changes typically reflect a concurrent evaluation of new conditions.”

What Should Auditors Keep in Mind as It Relates to Subsequent Events Disclosures Related to the COVID-19 Pandemic?

In complying with the requirements of AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*,¹ the overall objectives of the auditor are to

- obtain sufficient appropriate audit evidence about whether subsequent events are appropriately recognized and disclosed in the financial statements.
- respond appropriately to facts that become known after the audit report date that, had they been known to the auditor as of the report date, may have caused the auditor to revise the report.

AU-C section 560 defines subsequent events similarly to the definition in GASB Statement No. 56. It should be noted that in a state or local governmental financial statement audit, the auditor evaluates the reporting of subsequent events in relation to the fair presentation of the individual opinion units affected by the events.

Auditors will have to work with clients to ensure any subsequent events have been accurately identified and are properly reflected in the financial statements or notes to the financial statements as required by GASB Statement No. 56. If management is either unable or unwilling to identify those events and properly disclose or reflect them in the financial statements, this could result in a modification to the auditor’s opinion.

Refer to chapter 15 of AICPA Audit Guide *State and Local Governments* (the SLG guide), for more information about subsequent events.

Management’s Discussion and Analysis

Financial Reporting Considerations Related to the COVID-19 Pandemic

Governments may have a responsibility to discuss pandemic-related matters in management’s discussion and analysis (MD&A). GASB Statement No. 34, *Basic Financial Statements — and Management’s Discussion and Analysis — for State and Local Governments*, as amended, provides requirements for information in MD&A. MD&A should be confined to the specific items defined in

¹ All AU-C sections can be found in AICPA *Professional Standards*.

GASB Statement No. 34, one of which is a description of currently known facts, decisions, or conditions that are expected to have a significant effect on financial position or results of operations.

For governmental entities with fiscal years ending prior to the COVID-19 pandemic, MD&A would likely include information related to the pandemic in the discussion of currently known facts, decisions, or conditions expected to significantly affect financial position or results of operations. Currently known facts include information that management is aware of at the date of the auditor's report. Per GASB Implementation Guide (IG) 2015-1 question 7.5.14, the MD&A discussion of currently known facts should also address the expected effects on *both* the governmental and business-type activities. In addition, IG 2015-1 question 7.5.13 indicates the MD&A currently known facts should highlight but not repeat information that may be disclosed as subsequent events or contingencies in the notes to the financial statements. Further, question 7.5.13 states MD&A should not discuss the possible effects of events that *might* occur (although such matters could be addressed in the letter of transmittal) but instead discuss facts surrounding events that have already occurred.

For governmental entities with fiscal years ending after the commencement of the COVID-19 pandemic, MD&A would likely include information related to the pandemic throughout. The pandemic will generally affect analysis throughout MD&A, including discussions on financial position, results of operations, balances and transactions of specific funds, capital assets, and long-term debt activity, as well as the budget and currently known facts, decisions, or conditions.

[What Should Auditors Keep in Mind as It Relates to MD&A Related to the COVID-19 Pandemic?](#)

GASB Statement No. 34 requires that MD&A be presented as required supplementary information (RSI). AU-C section 730, *Required Supplementary Information*, addresses the auditor's responsibility with respect to RSI. As part of those responsibilities, auditors will need to compare the information presented in MD&A for consistency with (1) management's responses to the inquiries required by AU-C section 730 including whether the RSI has been measured and presented in accordance with prescribed guidelines, (2) the basic financial statements, and (3) other knowledge obtained during the audit of the basic financial statements. If MD&A departs materially from the prescribed guidelines, the auditor modifies the other-matter paragraph that refers to the RSI to include a statement that, although the auditor's opinion on the basic financial statements is not affected, material departures from the prescribed guidelines exist. The auditor then goes on to describe the departures. See chapters 2, 4, and 16 of the SLG guide for more information on RSI and the auditor's related responsibilities.

Looking for Example COVID-19 Pandemic MD&A Discussion, Financial Statement Disclosures, and Event-Based Disclosures?

The Municipal Securities Rulemaking Board (MSRB) has published a summary of disclosures submitted to the Electronic Municipal Market Access (EMMA) system made by issuers that reference the COVID-19 pandemic, which will be updated weekly. This document, "Municipal Securities Market COVID-19 Related Disclosure Detailed Spreadsheet," may serve as a resource to practitioners looking for examples of MD&A, financial statement subsequent event disclosures, and event-based disclosures, and may be accessed at <http://www.msrb.org/News-and-Events/COVID-19-Information.aspx>. Refer to the items listed in the Continuing Disclosures tab and disclosure subcategories "Audited Financial Statements or CAFR (Rule 15c2-12)" and "Event-Based Disclosures." Although looking to this resource for examples is useful to learn what other entities are doing, preparers and auditors are cautioned to ensure that MD&A and disclosures meet authoritative requirements.

Going Concern

Financial Reporting Considerations Related to the COVID-19 Pandemic

For the reasons cited in paragraph 18 of GASB Statement No. 56, going concern considerations are not typically a common occurrence in the governmental sector, particularly for general-purpose governments. However, the consequences of the COVID-19 pandemic are significant, and there may be more situations in which going concern considerations become relevant, especially for special-purpose governments with business-type activities only or business-type activities and fiduciary activities. With circumstances changing frequently due to the pandemic, management's evaluation of conditions or events that may have an effect on the entity's ability to continue as a going concern could be difficult, particularly for special-purpose governments.

GASB Statement No. 56, as amended, provides requirements for governmental entities related to going concern. Governmental entities have a responsibility to evaluate whether there is substantial doubt about their ability to continue as a going concern for 12 months beyond the financial statement date. If there is information that is currently known to the governmental entity that may raise substantial doubt shortly after this 12-month period (for example, within an additional 3 months), it also should be considered. These evaluations should not be performed on reporting units that constitute less than a legally separate entity.

GASB Statement No. 56, as amended, states that continuation of a legally separate governmental entity as a going concern is assumed in financial reporting in the absence of significant information to the contrary. Information that may significantly contradict the going concern assumption would relate to the following:

- A governmental entity's inability to continue to meet its obligations as they become due without substantial disposition of assets outside the ordinary course of governmental operations
- Restructuring of debt

- Submission to the oversight of a separate fiscal assistance authority or financial review board, or similar actions

The going concern considerations may be different for general-purpose governments versus special-purpose governments, especially those that have only business-type activities. GASB Statement No. 56, paragraph 18 indicates that a governmental entity's taxing power and borrowing capabilities combined with the unrelenting demand of public services may diminish the possibility of a governmental entity being unable to continue as a going concern. It also states that recurring operating losses may be common for some business-type activities (for example, transit operations, governmental health care organizations); however, the health and welfare needs of citizens may be reasons that these activities are subsidized by other governmental entities.

Going Concern — MD&A

As noted earlier, GASB Statement No. 34 requires a discussion in MD&A of currently known facts, decisions, or conditions expected to significantly affect financial position or results of operations. It may be necessary for governments to include a discussion of going concern issues in MD&A, depending on the facts and circumstances.

What Should Auditors Keep in Mind About Auditing Going Concern Assumptions and Disclosures Related to the COVID-19 Pandemic?

Auditors should refer to AU-C section 570, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, for requirements and guidance regarding the auditor's responsibilities relating to the entity's ability to continue as a going concern for a reasonable period of time and the implications for the auditor's report. It provides requirements and guidance regarding the adequacy of financial statement disclosure, the need to modify the auditor's report, communication with those charged with governance, and audit documentation concerning the auditor's going concern evaluation.

There are also going concern considerations from a governmental audit perspective that are outlined in chapter 15 of the SLG guide. For example, the auditor may consider whether other governments have a legal or moral responsibility to subsidize or otherwise provide financial support to the governmental entity being audited. Those subsidies could affect the auditor's going concern evaluation. In addition, state and local governmental entities may have access to federal funds to assist with providing public services as a result of the CARES Act and other federal funding provided in response to the COVID-19 pandemic.

Loss Contingencies and Claims and Judgments

Financial Reporting Considerations Related to the COVID-19 Pandemic

The GASB financial reporting framework does not currently have a separate standard on risks and uncertainties comparable to FASB *Accounting Standards Codification (ASC) 275, Risks and Uncertainties*. However, GASB does have requirements for contingencies and claims and judgments (as well as previously discussed subsequent events), which governments may increasingly encounter due to the effects of the pandemic.

Contingencies that may be affected by the current economic environment include loss contingencies associated with the collectability of receivables, guarantees of debt (including exchange, exchange-like, and nonexchange), unemployment compensation claims, and — subject to the guidance in GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions* — property tax appeals and tax refund claims. The applicable authoritative literature for these contingencies is included in GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, paragraphs 96–113, as amended and GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. Claims and judgments that may also be affected include the risk of loss from damage or destruction of assets, business interruption, and insurance recoveries, including recoveries associated with capital asset impairment. The applicable authoritative GASB literature for claims and judgments is included in GASB Codification Section C50, *Claims and Judgments*.

Chapter 8 of the SLG guide provides additional details on claims and judgments and loss contingencies.

[What Should Auditors Be Aware of as It Relates to Accounting and Financial Reporting of Loss Contingencies and Claims and Judgments Related to the COVID-19 Pandemic?](#)

For fiscal years ending prior to the COVID-19 pandemic, see the subsequent events discussion. For fiscal years ending after the commencement of the COVID-19 pandemic, GASB Codification Section C50 requires disclosures that focus primarily on risks of loss to which the government is exposed and contingencies that could significantly affect the amounts reported in the financial statements in the near term. The contingencies and claims and judgments addressed can stem from the extension of credit, guarantees of debt, and risk management. For example, the effects of the pandemic may meaningfully affect significant estimates related to accounts receivable allowances and self-insurance claims and increase the government’s probability of performing on a guarantee. Due to the effects of the pandemic, the necessity and robustness of the disclosures and the probability and amount of an accrual may require additional scrutiny by the auditor.

[Noncompliance With Finance-Related Legal or Contractual Provisions](#)

[Financial Reporting Considerations Related to the COVID-19 Pandemic](#)

The COVID-19 pandemic and subsequent downturn in the economy may have various effects on governmental entities’ compliance with legal and contractual provisions. For example, entities may violate the following:

- Debt covenants
- Minimum fund balance regulations
- State investment regulations
- Pension or other post-employment benefits (OPEB) funding requirements
- Continuing disclosure requirements, including event disclosures, as reported through EMMA
- Budgetary policies and regulations
- Provisions of federal financial assistance programs, which may be significantly increased due to pandemic-related federal funding

Paragraph 9 of GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, requires governmental entities to disclose significant violations of finance-related legal or contractual provisions and any actions taken to address these violations. The items listed previously may not materially affect financial statement amounts and disclosures of all governmental entities. Further, there may be categories of compliance requirements other than those in the preceding list for which noncompliance could materially affect financial statement amounts and disclosures.

What Should Auditors Be Aware of as It Relates to Noncompliance With Finance-Related Legal or Contractual Provisions as a Result of the COVID-19 Pandemic?

Auditors should follow the requirements in AU-C section 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*, which describes the auditor's responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements arising from noncompliance with provisions of laws and regulations. Because GASB requires governments to disclose significant violations of finance-related legal and contractual provisions, the auditor of a governmental entity should also be alert to the possible financial reporting effect of noncompliance that materially affects the financial statements and disclosures. For example, if a government violates a debt covenant, auditors will need to understand the implications of that covenant violation in terms of both the accounting implications and the audit reporting implications.

The SLG guide provides considerations related to noncompliance with laws and regulations in chapter 4. For auditors conducting an audit in accordance with *Government Auditing Standards*, the auditor has additional responsibilities related to noncompliance with laws, regulations, contracts, and grant agreements as discussed in chapters 3 and 4 of AICPA Audit Guide *Government Auditing Standards and Single Audits*, including a requirement to report noncompliance that has a material effect on the financial statements in the report issued under the requirements of *Government Auditing Standards*.

Are There Other Matters an Auditor Should Consider Related to a Government's Debt Other Than Debt Covenant Compliance?

Although each situation is different and should be evaluated based on its own specific facts and circumstances, the current environment has affected the debt securities market and may raise various issues pertaining to a government's credit rating. Auditors should consider whether a risk exists that the government's credit rating could be lowered and, if a risk exists, obtain an understanding of the effects that a reduced credit rating would have on the government's ability to fund its operations, or whether a reduced rating would affect the government's outstanding debt obligations or derivative instruments.

Municipal Securities Implications

Like all markets, the bond market has been affected by the COVID-19 pandemic. Currently, the MSRB is providing additional information on the effects of the pandemic on the market, including a municipal market trading report that is updated daily, which may be accessed at <http://www.msrb.org/News-and-Events/COVID-19-Information.aspx>. Additionally, the SEC has issued a public statement, *The Importance of Disclosure for our Municipal Markets*, that should be of interest to municipal issuers and auditors that are involved with exempt offering documents. In the statement, the SEC provides its views on the effects of the COVID-19 pandemic on the financial status of state and local governments and the importance of robust, timely, and accurate municipal issuer disclosure.

Fair Value of Investments

Financial Reporting Considerations Related to the COVID-19 Pandemic

The COVID-19 pandemic has had a negative effect on financial markets, which has led to fair value measurement and reporting questions. Estimating fair value requires significant judgment in normal circumstances. However, in the current environment, characterized by the potential for market volatility and an uncertain outlook, applying judgment in determining fair value may be even more challenging. GASB Statement No. 72, *Fair Value Measurement and Application*, provides the framework for measuring fair value for governmental entities. *Fair value* is defined in GASB Statement No. 72 as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” Paragraph 28 of GASB Statement No. 72 indicates that “if there is a quoted price in an active market for an identical asset or an identical liability, a government should use that quoted price without adjustment if measuring fair value, except as specified in paragraph 38.” In other words, if a security trades in an active market at the measurement date, its fair value will equal the quoted price.

GASB Statement No. 72 defines an *active market* as “a market in which transactions for an asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis” and does not provide bright lines or rules of thumb for what constitutes an active market. To assist entities with determining fair value in periods of market disruption, paragraphs 45–48 of GASB Statement No. 72 provide guidance on measuring fair value when the volume or level of activity for an asset or a liability has significantly decreased. In situations in which there has been a significant decrease in the volume or level of activity, it may be appropriate to consider other valuation techniques in estimating fair value.

Paragraph 49 of GASB Statement No. 72 lists the circumstances that may indicate a transaction is not orderly, whereas paragraph 50 provides guidance on how to consider such transitions.

Where Can an Auditor Find Guidance on Auditing Investments of State and Local Governments Valued at Fair Value?

Auditors should refer to AU-C section 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*, for requirements on testing how management values investments. Additionally, chapter 5 of the SLG guide provides additional detailed guidance from a governmental perspective.

Capital Asset Impairment Considerations

Financial Reporting Considerations Related to the COVID-19 Pandemic

Given the impact of the COVID-19 pandemic (operations disruptions, economic downturn), governmental entities may conclude that they should test their capital assets for impairment. The authoritative literature for capital asset impairment is found in GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, as amended. Determining whether a capital asset is impaired involves two steps: (1) identifying potential impairments and (2) testing for impairment.

Identifying Potential Impairments

Certain prominent events or changes in circumstances affecting a capital asset may indicate potential impairment. GASB Statement No. 42, as amended, describes five common indicators of impairment. Several of these indicators may be relevant in the pandemic environment as follows:

- Enactment or approval of laws or regulations or other changes in environmental factors
- A change in the manner or expected duration of use of a capital asset
- Construction stoppage or development stoppage

A change in demand for the services of a capital asset is not considered a separate indicator of impairment; however, the preceding indicators may be associated with changes in demand. When one of these indicators is present, governments should test capital assets for impairment. It is important to note, though, that if the capital asset is impaired and evidence demonstrates that the impairment will be temporary, a government should not write down the capital asset.

Testing for Impairment

When an indicator of impairment is present, the government should test for impairment by determining whether (a) the magnitude of the decline in service utility is significant and (b) the decline in service utility is unexpected. A decline in service utility is significant when the expenses associated with continued operation and maintenance (including depreciation) or costs associated with restoration of the capital asset are significant in relation to the current service utility. The decline in service utility is unexpected when the restoration cost or other impairment circumstance is not part of the normal life cycle of the capital asset. If the asset meets both impairment tests, a government should measure the amount of the impairment (that is, the portion of carrying value of the asset that should be written off).

Paragraph 12 of GASB Statement No. 42, as amended, provides three methods for measuring the amount of impairment if the government will continue to use the asset. The service units approach generally should be used to measure impairments resulting from enactment or approval of laws or regulations or other changes in environmental factors. The deflated depreciated replacement cost or the service units approach generally should be used to measure impairments identified from a change in manner or duration of use. For impaired capital assets that a government will not continue to use and for capital assets impaired from construction or development stoppage, the government should report the assets at the lower of carrying value or fair value.

Chapter 7 of the SLG guide provides additional description of the accounting requirements for capital asset impairments.

[What Are the Auditing Considerations for Capital Asset Impairments in the State and Local Government Arena?](#)

In accordance with AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, an auditor should obtain an understanding of internal controls relevant to capital assets, including procedures that ensure the proper calculation and recording of capital asset impairments. In addition, the auditor should perform procedures to evaluate whether capital asset impairments have been properly reported.

[Termination Benefits](#)

[Financial Reporting Considerations Related to the COVID-19 Pandemic](#)

The COVID-19 pandemic is resulting in a decrease in revenues (for example, income tax, sales tax, hotel tax) for many governmental entities. These revenue decreases may prompt the need for cost-cutting measures, such as workforce reductions or requests for early retirements. GASB Statement No. 47, *Accounting for Termination Benefits*, as amended, requires employers to recognize a liability and expense for voluntary termination benefits (such as early retirement incentives) when the offer is accepted and the amount can be estimated. Employers should recognize a liability and expense for involuntary termination benefits (such as severance benefits) when a plan of termination (as defined in the statement) has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees, and the amount can be estimated. Governmental fund financial statements should recognize those liabilities and expenditures to the extent the liabilities are normally expected to be liquidated with expendable available financial resources. When termination benefits include enhancement of pensions or OPEB provided under an existing defined benefit pension plan or OPEB plan, the provisions of GASB Statement Nos. 68, 73, or 75, as amended, as appropriate, should be applied. GASB IG 2015-1 questions Z.47.1–Z.47.2, as amended, and appendix BZ-1 provide examples of how to compute the liability and expenses for termination benefits using various assumptions.

Extraordinary and Special Items

Financial Reporting Considerations Related to the COVID-19 Pandemic

Many have asked whether events related to the COVID-19 pandemic constitute extraordinary or special items. According to paragraph 56 of GASB Statement No. 34, special items differ from extraordinary items in two ways. Special items should be within the control of management and are required to be only unusual in nature or infrequent in occurrence, but not both. Conversely, extraordinary items are not required to be within the control of management but are required to be both unusual in nature and infrequent in occurrence. Paragraphs 45–50 of GASB Statement No. 62 provide guidance for special and extraordinary items and include the following criteria that should be met to classify an event or transaction as either unusual in nature or infrequent in occurrence.

- *Unusual in nature.* The underlying event or transaction should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the government, taking into account the environment in which the government operates.
- *Infrequent in occurrence.* The underlying event or transaction should be of a type that would not reasonably be expected to recur in the foreseeable future, taking into account the environment in which the government operates.

GASB is expected to address this question as it relates to certain new pandemic-related federal funding in a technical bulletin expected to be issued by July 2020. Watch GASB's website (www.gasb.org) for the final technical bulletin. See also the earlier "GASB Resources" section for more information.

Operating Versus Nonoperating for Proprietary Funds

Financial Reporting Considerations Related to the COVID-19 Pandemic

The COVID-19 pandemic environment has created unique circumstances that have many governments and auditors questioning whether certain transactions should be classified as operating or nonoperating in the proprietary fund resource flows statement (for example, federal funds received or payroll costs incurred during a furlough).

There are many nuances, facts, and circumstances that need to be considered by governments in making the operating versus nonoperating determination for both revenues and expenses. Our initial analysis suggests the conclusions reached in this area will not be uniform for all governmental entities' operations. In other words, some activities as a result of the pandemic will be classified as operating, whereas other activities would more properly be classified as nonoperating.

The GASB staff is expected to address this question as it relates to certain new pandemic-related federal funding in a technical bulletin expected to be issued by July 2020. Watch GASB's website (www.gasb.org) for the final technical bulletin. See the earlier "GASB Resources" section for more information.

Tax Revenue — Delayed Due Dates

Financial Reporting Considerations Related to the COVID-19 Pandemic

In an effort to provide relief to taxpayers, some governmental entities are providing a one-time delay of the due date for taxes. In some of these situations, delay of the due dates is resulting in the receipt of those payments outside of the typical 60-day availability period, which has many preparers and auditors questioning whether governmental funds may recognize the tax revenue for those payments received outside of the 60-day availability period. GASB literature addresses this situation in paragraph 8 of NCGA Interpretation No. 3 (or GASB Codification Section P70.104) and indicates that “if, because of unusual circumstances, the facts justify a period greater than 60 days, the governmental unit should disclose the period being used and the facts that justify it.”

Pension and OPEB Valuations

Financial Reporting Considerations Related to the COVID-19 Pandemic

GASB’s various standards for pension and OPEB plans discuss the need for actuarial valuations and the required timing for such valuations. These standards discuss the need for update procedures to roll forward a plan’s most recent fiscal year-end amounts from actuarial valuations that were performed earlier than the plan’s most recent fiscal year-ends. GASB standards also emphasize that if update procedures are used and significant changes occur between the *actuarial valuation date* and a plan’s fiscal year-end, professional judgment should be used to determine the extent of procedures needed to roll forward the measurement from the actuarial valuation to the plan’s fiscal year-end, and consideration should be given to whether a new actuarial valuation is needed. These GASB requirements will need consideration by governments in light of the potential impact of the COVID-19 pandemic.

From an audit perspective, audit procedures in this area may include reviewing the appropriateness of the government’s update procedures to roll forward the total pension liability to the plan’s fiscal year-end and determining whether all significant known events have been properly included.

Audit-Specific and Auditor-Reporting-Specific Matters

At the time of the issuance of this document, various parts of the country were in various stages of reopening, with some lifting stay-at-home orders and some continuing such orders. Additionally, some governmental entities and audit organizations may continue work-at-home policies regardless of the rules in effect externally. Although information in this section on remote working environments may no longer be applicable to some auditors, it is being provided for those auditors who continue to experience restrictions.

Planning Meetings

How Should Auditors Perform Audit Planning When It Needs to Occur Remotely?

The first standard of fieldwork indicates that “the auditor must adequately plan the work and must properly supervise any assistants.” Auditors should take note that remote working is not an excuse to

not have required audit planning meetings. Auditors should ensure they are still holding these discussions as needed and having substantive discussions on engagement risks with the engagement team prior to commencing audit fieldwork.

Fraud Inquiries

What About Fraud Risk During These Uncertain Times?

Auditors should be on higher alert for fraud risks given these uncertain times. For governments that have laid off key personnel, and with work forces moving out of the typical office environment, there could be a breakdown in internal control. Auditors may need to adjust audit procedures as necessary to help appropriately address any potential fraud risks that could have a material effect on the financial statements.

What if the Auditor Is Unable to Conduct Fraud Interviews in Person With the Client Due to the Impacts of the COVID-19 Pandemic?

AU-C section 240, *Consideration of Fraud in a Financial Statement Audit*, lays out a number of requirements and procedures that may be more challenging in a remote audit. For example, auditors will still need to carry out an appropriate discussion among the engagement team in order to understand what fraud risk factors may be affecting the entity in this environment. Paragraph .A17 of AU-C section 240 indicates that inquiries of management and others within the entity are *generally* most effective when they involve an in-person discussion. However, due to the current circumstances related to the pandemic, these inquiries could be done via videoconferencing technology. The key consideration is whether the manner in which the inquiries are made allows the auditor to “read the body language” of the person to whom the inquiries are directed. So, when fraud interviews cannot be performed in person, use of videoconferencing would be preferable to audio-only conferencing because auditors would be able to see body language.

Risk Assessment

How Will the Auditor’s Risk Assessment Be Affected for Audit Periods Affected by the COVID-19 Pandemic?

Identifying, assessing, and responding to risks of material misstatement are at the core of every audit. AU-C section 315 establishes requirements regarding the auditor’s responsibility to identify and assess the risks of material misstatement in the financial statements. The pandemic will likely affect many aspects of the risk assessment process, including the understanding of the entity and environment, internal control consideration and testing, identification of risks, and responding to those risks. An additional factor for governmental audits is that the risk assessment process considers each opinion unit. Auditors should also remember that the risk assessment process occurs throughout the audit and that the results of the pandemic may alter the initial risk assessments made.

Access to Books and Records

What if the Auditor Has Trouble Gaining Access to the Client's Books and Records During the Pandemic?

During the pandemic, accessing client books and records may present hurdles for some auditors, especially in cases in which clients still maintain mostly paper records. Auditors may be able to obtain client-prepared copies or scans of key records, but auditors need to consider the authenticity of those records and perhaps perform additional audit procedures to be satisfied that those records are complete, accurate, and authentic.

In cases in which auditors are unable to access client books and records, auditors may have to inform clients that audits cannot be completed until books and records can be accessed and discuss the potential impact on any relevant filing deadlines. (See the "Managing Filing Deadlines" section later for further discussion.)

Internal Control Over Financial Reporting

What Should Auditors Be Thinking About in the Financial Statement Audit With Regard to a Client's Internal Control Over Financial Reporting?

In this ever-changing and somewhat unstable environment, auditors should inquire about any changes in the client system of internal control due to the pandemic and encourage clients to document any control changes made. The controls and procedures may have changed dramatically to accommodate remote work forces and process flows. There are likely different systems of internal control (entirely different or at least partially different) that have been in effect and operating during the audit period. Even for audits of fiscal years ending prior to the COVID-19 pandemic, the internal controls for closing the books, preparing journal entries, and preparing the financial statements may have changed as many of those processes occur after year-end.

The auditor needs to obtain an understanding of controls in place prior to and during any pandemic disruptions; however, the auditor should maintain an appropriate perspective on this matter. The length of time that new controls may have been in place and the level of activity that occurred during that time will drive the importance of gaining an understanding of the new controls and determining the controls relevant to the audit.

If client sites are closed and auditors are unable to perform audit procedures on-site, performing walk-throughs and certain tests of internal control will be challenging. Auditors may need to think innovatively and use videoconferencing technology to make inquiries and observe certain controls. For example, an auditor can ask client personnel to enter passwords to access the accounting system. Using a video feed, the auditor can still observe whether those passwords were successful or locked out the employee.

An understanding of internal control assists auditors in identifying types of potential misstatements and factors that affect the risks of material misstatement and in designing the nature, timing, and extent of further audit procedures. Even when auditors have no plans to rely on the operating effectiveness of controls in the financial statement audit, auditors are still required to obtain an

understanding of internal control relevant to the audit and to determine that those controls have been implemented. Obtaining an understanding of controls may be achieved remotely; however, inquiry alone is not sufficient to determine whether such controls have been implemented. As such, auditors need to consider what evidence can be obtained remotely to determine whether effectively designed controls have been placed in operation. Auditors may not be able to rely on controls in all cases and may have to change the nature and increase the extent of substantive audit procedures. Additionally, if auditors are unable to obtain sufficient, appropriate audit evidence to perform and complete the risk assessment process, then auditors may have scope limitations significant enough to result in report modifications.

For auditors conducting an audit in accordance with *Government Auditing Standards*, the auditor has additional reporting responsibilities beyond those requirements in AU-C section 265, *Communicating Internal Control Related Matters Identified in an Audit*, related to internal control over financial reporting as discussed in chapter 4 of AICPA Audit Guide *Government Auditing Standards and Single Audits*, including a requirement to report material weaknesses and significant deficiencies in the report issued under the requirements of *Government Auditing Standards*.

Additional guidance related to internal controls is available in the *Journal of Accountancy* article "[Tips for auditing with changed controls during the pandemic.](#)"

Inventory Observations

Many governmental entities' inventory balances are immaterial. For those governmental entities that have material inventory balances, the considerations relating to performing inventory procedures remotely are generally the same as for other types of entities. Refer to the guidance on this topic provided in the [AICPA's A&A FAQs related to COVID-19 issues, 2nd edition](#) for more information

Use of External Confirmations

How Should Auditors Handle Situations in Which Responses to Account Confirmations Might Be Limited Due to the COVID-19 Pandemic?

As noted in AU-C section 505, *External Confirmations*, depending on the circumstances of the audit, audit evidence in the form of external confirmations received directly by auditors from confirming parties may be more reliable than evidence generated internally by the entity. In cases in which a client site has been shut down or key staff are no longer on-site, obtaining external confirmations could be an alternative way to obtain audit evidence. However, there could be situations in which those audit confirmations are not completed and sent back to the auditors, perhaps due to the respondent's office closures. In such cases, auditors would have to design additional audit procedures to gain sufficient, appropriate audit evidence related to the relevant assertions for the particular account balance or class of transaction for which confirmation was requested.

Typically, if auditors are able to design and perform additional tests of those relevant assertions, nonreceipt of confirmations in and of itself should not result in a scope limitation. However, if auditors are unable to obtain sufficient audit evidence through performing audit procedures on the client books and records and are relying on receipt of audit confirmations as a key source of audit evidence, the

nonreceipt of those confirmations could result in a scope limitation (when balances are material to the financial statements).

Is It Permissible for Auditors to Send Electronic Account Confirmations in Lieu of Traditional Paper Ones?

Due to increasing business closures and movement to telecommuting models, auditors may consider sending electronic confirmations rather than paper confirmations. Some firms may have process flow software that allows this to be done quite easily, and it might result in a better response rate. Asking clients to contact their vendors and suppliers in advance may be prudent to understand the best way to contact these parties in the current environment. Additionally, auditors should be aware that although oral confirmations may be the fastest and most effective way to obtain evidence about account balances, they would be considered akin to an inquiry of a third party. In considering procedures, firms also should consider that, given sensitivity to cash flow in certain parts of the economy, more accounts receivable may remain outstanding when audit procedures are performed than in prior audits.

Managing Filing Deadlines

Governments are often subject to financial reporting and other filing deadlines that may be affected by the COVID-19 pandemic. Auditors will need to work with their governmental clients to evaluate financial statement and other filing deadlines and whether they can be met (for example, state-mandated or federally mandated deadlines, EMMA deadlines, Government Finance Officers Association certificate program deadlines). In some cases, filing deadlines have been extended or leniency is being provided. The AICPA's Governmental Audit Quality Center has accumulated some known [pandemic-related deadline extensions of audited financial statements and other reports](#). In cases in which extensions have not been issued, auditors may want to encourage clients to contact the applicable regulatory and other entities to see if waivers or extensions can be obtained.

Management Representation Letters

Should Auditors Be Adding Additional Representations Related to the COVID-19 Pandemic to the Management Representation Letter?

During this pandemic, additional representations may be added to the management representation letter, depending on the particular circumstances of an engagement. Those additional representations may relate to subsequent events, going concern, claims and judgments, termination benefits, fraud, and significant estimates, among others.

Additional management representation letter considerations are provided in chapter 15 of the SLG guide.

What if My Client Is Unable to Provide the Signed Original Management Representation Letter With an Original Signature on Company Letterhead?

Using electronic means to obtain signed management representation letters is acceptable if auditors can obtain appropriate evidence of management's receipt and acknowledgment of the representations — in other words, confirmation that the signatory knowingly and willingly signed the representation

letter. Whether auditors accept electronic signatures, scanned images of signatures, and so on, is a matter of firm risk management practices as well as applicable state laws or regulations addressing legal acceptability of electronic signatures.

One question asked regularly is whether it is acceptable for management representation letters to be on “plain paper” rather than on company letterhead. The standards do not require use of client letterhead. This, again, is a matter of firm risk management practices.

What if My Client Is Unable to Provide Certain Representations in the Management Representation Letter?

Depending on what is omitted from management’s representation letter, the failure to obtain all representations does not necessarily result in a scope limitation. If management does not provide one or more of the requested written representations, auditors should do the following:

- Discuss the matter with management.
- Reevaluate the integrity of management and evaluate the effect this may have on the reliability of representations (verbal or written) and audit evidence in general.
- Take appropriate actions, including determining the possible effect on the opinion in the auditor's report in accordance with AU-C section 705B, *Modifications to the Opinion in the Independent Auditor's Report*.

Emphasis-of-Matter Paragraphs and Types of Auditor’s Reports

Should Auditors Be Including Emphasis-of-Matter Paragraphs Related to the COVID-19 Pandemic in Their Audit Reports?

Auditors may conclude that an event has such a material impact on an opinion unit that it would be appropriate to include an emphasis-of-matter (EOM) paragraph in the auditor’s report to direct the reader’s attention to the event and its effects. As paragraph .06 of AU-C section 706B, *Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor’s Report*, notes, EOM paragraphs are included in the auditor’s report if the auditor considers it necessary to draw users’ attention to a matter appropriately presented or disclosed in the financial statements that, in the auditor’s professional judgment, is of such importance that it is fundamental to users’ understanding of the financial statements.

Paragraph .A2 of AU-C section 706B indicates that a major catastrophe that has had, or continues to have, a significant effect on the financial position of an entity (opinion unit in the governmental arena) is an example of circumstances when auditors may consider it necessary to include an EOM paragraph. Whether the COVID-19 pandemic constitutes a major catastrophe for a governmental entity is a matter of the auditor’s professional judgment.

What if the Auditor Encounters Situations in Which an Unmodified Opinion on an Opinion Unit is Not Appropriate? What Type of Opinion Should Be Issued?

In situations in which auditors encountered material uncorrected misstatements of the financial statements of an opinion unit or scope limitations of an opinion unit, auditors may find the following table from paragraph .A1 of AU-C section 705B helpful.

<i>Nature of Matter Giving Rise to the Modification</i>	<i>Auditor's Professional Judgment About the Pervasiveness of the Effects or Possible Effects on the Financial Statements</i>	
	<i>Material but Not Pervasive</i>	<i>Material and Pervasive</i>
Financial statements are materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

In discussing government-specific audit considerations, paragraph .A18 of AU-C section 705B indicates that because an auditor of a state or local government entity expresses an opinion or disclaims an opinion for each opinion unit, an auditor report may include an unmodified opinion with respect to one or more opinion units and a modified opinion for one or more other opinion units.