



INSIGHTS FROM THE BDO CENTER FOR HEALTHCARE EXCELLENCE & INNOVATION

# ACCOUNTING, AUDIT AND OTHER COMPLIANCE CONSIDERATIONS FOR HEALTHCARE PROVIDERS RELATED TO COVID-19

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## At A Glance

Providers continue to focus most on the critical patient implications of COVID-19, but they must also consider questions about the broader implications for their business. In the face of further uncertainty ahead, healthcare leaders can take steps now to mitigate the impacts of the pandemic on their business so that they can prepare to reestablish full patient care services and be better prepared for additional waves of the virus outbreak that might take place.

Healthcare leaders can look to their CFO and senior financial executives for guidance on critical accounting, financial reporting and operational decisions that can help position the organization to sustain through the crisis and thrive in its wake. This FAQ answers specific questions about key financial reporting and accounting issues healthcare leaders must consider, including the pandemic's impact on revenue recognition, lease accounting and debt, and actions to take ahead of the 2020 financial reporting period—and beyond it.

**NOTE: For further discussion and guidance around financial relief available to your specific organization, we recommend contacting your assigned grants management officer and program official.**

## Uniform Guidance Funding

### Will additional Uniform Guidance funding come into play or can it be rolled out through Medicaid costs?

Consistent with existing practice, states have an opportunity at any time throughout each quarter to request additional funding from the Centers for Medicare & Medicaid Services (CMS) as necessary to cover expenditures for allowable Medicaid administrative and service costs, including expenditures resulting from amendments made by section 6004 of the Families First Coronavirus Response Act. Should any state need additional funds before the end of a quarter, they should request them through a supplemental grant award request to the extent that the state and its expenditures are allowable, and the state has a permissible source of non-federal share. CMS will evaluate such requests and issue any appropriate additional supplemental grant awards.

The Families First Coronavirus Response Act included a temporary increase in the Medicaid federal medical assistance percentage (FMAP) from Jan. 1, 2020 through the emergency period. The 6.2 percentage point increase does not apply to the expansion group. To be eligible for the funds, states cannot implement more restrictive eligibility standards or higher premiums than those in place as of Jan. 1, 2020, must provide continuous eligibility for enrollees through the end of the month of the emergency period, and cannot impose cost sharing for COVID-19-related testing and treatment services including vaccines, specialized equipment or therapies.

In terms of grant funding opportunities, CMS is issuing emergency notice of funding opportunities (NOFOs) related to COVID-19 but not necessarily to reimburse increased Medicaid costs. Applicants may search for applicable funding opportunities [here](#). For further discussion and guidance on funding, please contact your assigned grants management officer and program official.

From a compliance perspective, the American Institute of Certified Public Accountants has also requested that the Office of Management and Budget (OMB) provide further clarification on what COVID-19 relief funds the Single Audit guidelines will impact.

### Are we required to track our COVID-19 expenditures in a separate cost center for Single Audit purposes?

The OMB has not explicitly communicated such a requirement, but funding agencies such as the Centers for Disease Control and Prevention (CDC) have issued guidance requiring recipients to maintain records and documentation to

substantiate the cost. At the very least, organizations need to implement tracking mechanisms for COVID-19 expenditures related to federal awards so they can be mapped to the correct associated federal awards for Single Audit purposes.

For operational, forecasting and other business purposes, hospitals, health systems and physician groups should separately track all COVID-19 expenditures incurred as best they can. As possible, we recommend organizations segregate costs associated with the pandemic by identifying a cost center to charge items procured specifically in response to COVID-19 preparation and response. This may include:

- ▶ Setting up COVID-19 units to capture all associated costs.
- ▶ If unable to segregate costs, healthcare organizations should ensure they properly code COVID-19 cases as outlined below to develop an allocation method to identify estimated costs for patients and resources.

Organizations can use the CDC's Disaster Preparedness Budget model to anticipate, respond and recover from catastrophic events. The model outlines different buckets of expenses healthcare organizations should strive to identify for reimbursement. This model can be adopted to track expenses in different categories. No guidance has been given at this time on whether the Department of Health and Human Services (HHS) will use this model, but the agency has recommended that hospitals and physicians follow it for now.

## Contract Compliance

### How should my organization handle contract compliance reporting if we've had to divert our original intended purposes to another COVID-19 related purpose?

If contracts are adjusted to address a COVID-19 related purpose that is separate from the original intended purpose of the contract, contract compliance reporting impacts may vary. For instance, the CDC has noted that a redirection of funds may be allowed when the funds being redirected are within the scope of the current award and the award's statutory authority, without duplicating other federally funded activities. And so, although the OMB has not yet released official instruction, you can likely address contract compliance reporting through that original award reporting requirements, unless the scope of the current award does not line up with the new intended purpose.



## Federal Emergency Management Agency (FEMA) Grants Management

[What are the details and compliance measures for obtaining grant funding from FEMA?](#)

In response to COVID-19, President Trump declared a national emergency on March 13, 2020 to activate federal assistance and provide financial relief to hospitals and other healthcare organizations based on the Stafford Act. This declaration also allows the Trump administration to activate FEMA to assist state and local governments in the following ways:

- ▶ Provide up to \$45 billion to states to combat COVID-19
- ▶ Allow states to request 75% federal cost-share for COVID-19 related expenses. (This requires execution of a FEMA-state agreement, and local governments can apply through their respective states. No assistance can be duplicative to services provided by HHS or CDC.)
- ▶ Services eligible for FEMA assistance include the following:
  - Management, control and reduction of immediate threats to public health and safety
  - Emergency medical care
  - Use of specialized equipment
  - Medical waste disposal
  - Emergency medical transport
  - Medical sheltering

FEMA funding, separate from the \$30 million that HHS began delivering to healthcare providers on April 10, 2020 based on a Medicare fee-for-service formula, is available through a reimbursable grant program.

See [FEMA's website](#) for a more detailed list of services eligible for assistance.

## Government Relief Packages

[We're planning to apply for federal relief. What reporting measures do we need in place?](#)

Hospitals, health systems and physician groups should be prepared to understand, and document expenses incurred, as well as lost revenues associated with deferred or cancelled procedures or visits, in anticipation of the ability to access numerous funding sources. These funding sources include direct federal aid (through FEMA, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) and federal matching programs), bank loans against promised federal support, business interruption insurance claims and other funding mechanisms.

As possible, organizations should be able to report expenses and lost revenue related to COVID-19. We recommend segregating costs associated with the pandemic by identifying a cost center to charge items procured specifically in response to COVID-19 preparation and response. This may include:

- ▶ Setting up COVID-19 units to capture all associated costs.
- ▶ If unable to segregate costs, healthcare organizations should ensure they properly code COVID-19 cases as outlined below to develop an allocation method to identify estimated costs for patients and resources.

Organizations can use the CDC's Disaster Preparedness Budget model to anticipate, respond and recover from catastrophic events. The model outlines different buckets of expenses healthcare organizations should strive to identify for reimbursement. This model can be adopted to track expenses in the different categories. No guidance has been given at this time on whether the HHS will use this model, but the agency has recommended that hospitals and physicians follow it for now.

## Accounting & Financial Reporting

### What types of financial statement disclosures does my organization need to make?

ASC 855, *Subsequent Events*, requires entities to evaluate events after the balance sheet date. The accounting and disclosures an entity will need to consider depend on its financial year-end date. The World Health Organization (WHO) did not announce the coronavirus as a global health emergency until Jan. 30, 2020, which prompted national governments to begin putting actions in place to slow the spread.

For 2019 calendar year-end entities, the effects of the coronavirus represent a subsequent event that is not expected to impact amounts recognized in the year-end financial statements (i.e., a non-recognized subsequent event). When a healthcare entity has known material curtailments after the balance sheet date but prior to the issuance of its financial statements, then the entity would likely need to disclose those matters to fairly present the financial statements in a way that provides investors or other stakeholders the material information. Such known curtailments may include, but are not limited to, one or more of the following:

- ▶ Significant reductions in patient volume or cancellation of significant contracts.
- ▶ Suppliers' inability to provide the medical supplies necessary to carry out patient-related services.
- ▶ Inability to perform ordinary reporting, administrative or other functions due to workforce constraints.
- ▶ Cash flows materially altered in the period subsequent to year-end because of government action or shutdowns of certain facilities.
- ▶ Liabilities subject to debt covenants that the entity can no longer meet due to changes in cash flow or inability of the entity to provide financial information and reporting required by the debt agreement.
- ▶ Impacts of government actions such as the Defense Production Act of 1950, which grants the federal government the power to direct the activities of a U.S.-based business.
- ▶ Impacts from asking for government assistance or conditions attached to such assistance.
- ▶ All of the above factors should be considered in an entity's going concern analysis under ASC 205-40, *Presentation of Financial Statements – Going Concern*.

### What is the rationale behind the emphasis of matter (EOM) paragraph to the auditor's opinion on the financial statements?

U.S. Generally Accepted Accounting Principles (U.S. GAAP) requires entities to disclose significant risks and uncertainties, as well as subsequent events. In addition, the auditor may consider it necessary to draw users' attention to these disclosures by emphasizing the significant uncertainties or the unusually important subsequent events in the auditor's report. The purpose of an EOM paragraph is to draw attention to a matter or matters presented or disclosed in the financial statements that are of fundamental importance to understanding the financial statements.

COVID-19 has either already significantly impacted the operations of entities subsequent to year-end or it could significantly impact such operations. The extent, however, may be unknown given the timing of the audit report release date. With the pandemic in mind, auditors will consider adding an EOM paragraph when an entity has experienced a direct material impact or expects to experience a direct material impact. As a result, auditors may use the EOM paragraph to either highlight a going concern uncertainty or reference the subsequent event disclosure which further discloses the effect of COVID-19 on the entity after the balance sheet date.

## Accounts Receivable Valuation

### What should my organization do when estimating collectability of the receivables during the temporary downturn? What changes in cashflow projections can we see from payers in the future?

Companies' estimation methodologies need to consider all information available including historical, current and forecasted. Companies will need to ensure that their admission policies and related internal controls over the classification of patients into financial classes are appropriately designed and implemented to ensure that their estimation methodologies are properly capturing the economic impacts of changes in patient health insurance coverage and ultimate ability to pay. Companies will need to consider establishing additional financial classes for patients who may be unemployed or temporarily out of work. They also need to consider reimbursement rates for COVID-19. Note that providers are to treat all COVID-19 patients as in-network patients and providers cannot collect any out-of-pocket expenses in an amount greater than what the patients would have paid if they were in-network.

Changes to cash flow projections from payers depend on changes in the marketplace and underlying demographics of payers' insured populations. Due to the continually evolving nature of the COVID-19 crisis, the nature and extent of changes to cash flows may be unclear and may need to be reevaluated frequently.

## Revenue Recognition

### What's changed in how my organization should report revenue recognition?

Revenue recognition guidance under ASC 606, *Revenue from Contracts with Customers*, remains the same. However, changes in the underlying current and forecasted insured populations may materially impact your organization's historical collection experience, which you use in the estimate of the variable consideration.

### What compliance issues does my organization need to watch out for if clients are recording revenue using telehealth (i.e., those that could equate to increased denials, recoupments, audits or other actions)?

Compliance issues to watch out for include making sure your organization establishes the medical necessity for the virtual visit and proper coding for the telehealth services. The documentation and coding requirements may overlap or conflict with face-to-face visits resulting in confusion, miscoding or and ultimately, denials.

### Under ASC 606, do we still consider nonpayment of co-pays or deductibles as price concessions or are they now true bad debts, given that many people have lost their jobs because of the pandemic?

The determination of whether an organization has provided an implicit price concession is made at contract inception based

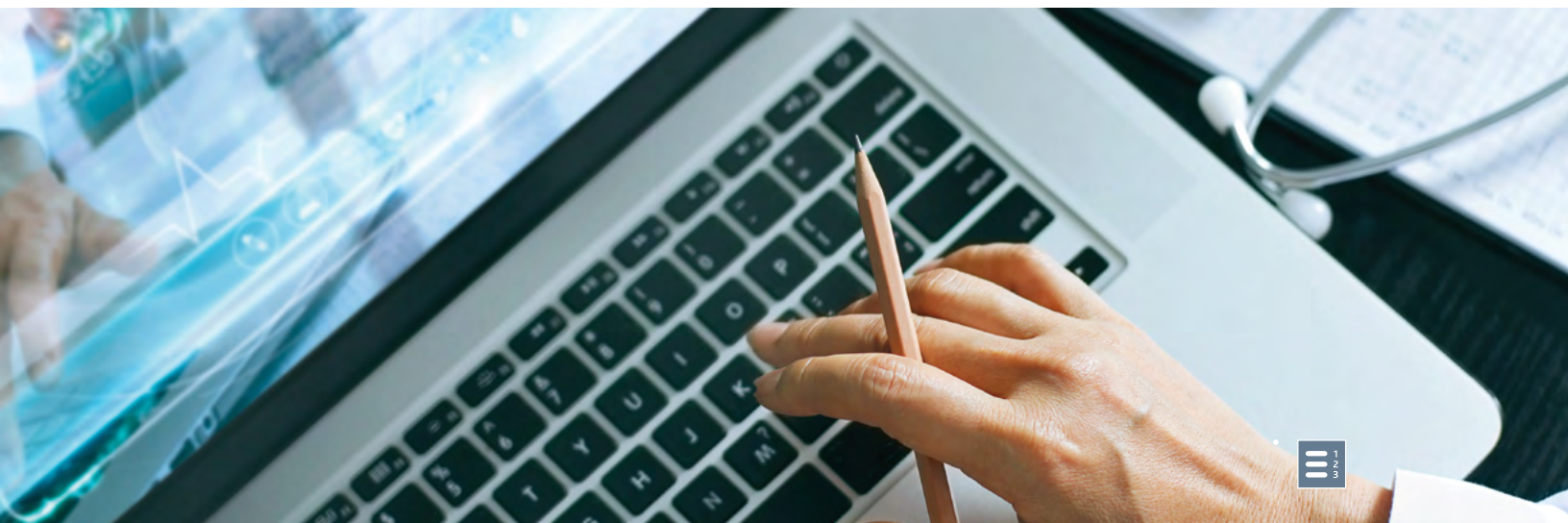
on facts and circumstances. The emergence of COVID-19 will not impact the organization's revenue recognition policy, including the implicit price concession versus credit loss determination. When the organization subsequently collects significantly less than its original estimate of variable consideration, there may be facts and circumstances that indicate there has been an adverse change in the patient's credit worthiness (for example, the patient filed for bankruptcy or lost their job because of COVID-19), and the difference may be better classified as an impairment loss (bad debt) rather than a change in the transaction price. The organization is required to update its estimate of the transaction price at the end of each reporting period and should not wait for subsequent cash collections to do so.

### We have adopted ASC 606 at our hospital. How do we assess the variable consideration required for Step 3-Determining the Transaction Price, for COVID-19 cases? Should we separately evaluate COVID-19 patient receivables in a portfolio approach under this step?

Portfolio approaches are typically payer-based, so the reimbursement for services rendered is based on payer-specific reimbursement rates and historical collection experience. Therefore, it would be inappropriate to classify all COVID-19 patients in the same portfolio if the expected reimbursement is going to come from different sources using different reimbursement rates. Note that providers are to treat all COVID-19 patients as in-network patients, and providers cannot collect any out-of-pocket expenses in an amount greater than what the patients would have paid if they were in-network.

### What steps of ASC 606 is COVID-19 most likely to impact?

Step 3 – Determining the Transaction Price, which includes variable consideration.





## Accrued Severance

### What are the accounting rules around recognition of severance costs?

ASC 712-10-25-1 notes that organizations should recognize non-retirement post-employment benefits offered as special termination benefits to employees as a liability and a loss when the employees accept the offer and the organization can reasonably estimate the amount. An employer that offers special termination benefits to employees for a short period of time shall not recognize a loss at the date the offer is made based on the estimated acceptance rate.

ASC 712-10-25-2 states that an employer that provides contractual termination benefits shall recognize a liability and a loss when it is probable that employees will be entitled to benefits and the amount can be reasonably estimated. The cost of termination benefits recognized as a liability and a loss shall include the amount of any lump-sum payments and the present value of any expected future payments.

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## Contract Compliance

### My organization is experiencing cash flow challenges because of cancelled elective and non-urgent surgeries. How should we structure new debt or financing agreements? How should we handle existing contractual arrangements? Do we need to substantially modify or extinguish contracts?

COVID-19 has forced all businesses to rethink contracts and compliance.

Before structuring new debt or financing agreements, we recommend:

1. Analyzing immediate and near-term cash flow needs, what cost reduction measures your organization can take, and what other relief is available. Certain contracts like management service agreements (MSAs) and others may contain penalties if providers are unable to meet certain volumes or metrics. Your organization should include such penalties within related cash flow considerations.
2. Evaluating cash flows against current contract arrangements to determine what near-term financial arrangements your organization needs.
3. Working with management to determine compliance with state and federal laws and regulations, including contracts, debt agreements, staffing and other matters.
4. Analyzing cash flows, determining potential non-compliance with financial and affirmative covenants, evaluating both the financial covenants and operating ratios that are components of those agreements, as well as any affirmative covenants, for debt agreements.
5. Remaining aware of volume or staffing commitments that are embedded within certain contractual agreements while cutting costs and other cash flow measures. Fiscal management should work hand in hand with legal and compliance teams to ensure that the organization can still meet compliance metrics with a potentially reduced workforce.

For any debt modifications and/or restructurings for entities that are not lending institutions, U.S. GAAP related to ASC 470-50, *Debt Modifications and Extinguishments*, still applies.



## Going Concern

Our organization owns an assisted living company and is planning to issue its Dec. 31, 2019 financial statements during May 2020. We are in the process of renegotiating our mortgages that are all due within 12 months of our year's end. These mortgages are all current in our financial statements. What do we need to consider in our going concern analysis to properly address going concern under ASC 205-40?

While you are in the process of renegotiating mortgages currently due, unless and until you finalize the agreements with new terms, the related cash outflows should be considered within the cash flow projections supporting the going concern analysis for 12 months from the report issuance date.

## Going Concern With Liquidity

Are the impacts of COVID-19 material to management's assessment of our ability to continue as a going concern?

When assessing future conditions, both quantitative and qualitative information needs to be considered as of the date the financial statements are issued. Organizations should analyze such conditions for a period not exceeding one year subsequent to the report issuance date every reporting period. Management should look at a variety of factors to assist in evaluating the entity's sustainability and the ability to manage obligations due within a year.

COVID-19 has significantly impacted industry revenues, and therefore cash flows. Accordingly, organizations need to update any projections they used to support the Going Concern assumption as of year-end to reflect the current cash flow impact, as well as the projected impact as the economy reopens.

Adjustments to forecasts also need to contemplate matters such as:

- ▶ Revisions to significant estimates such as allowances and valuations of inventory, which may impact future cash flows based on reductions in a consumer's ability to pay or a customer's need for supplies.
- ▶ The impact of COVID-19 on a market or geography that may be material to operations.
- ▶ Any Small Business Administration (SBA) financing, as well as the likelihood of forgiveness and/or repayment.

- ▶ CARES Act Provider Relief Fund payments and the impact on cash flows.
- ▶ CMS Accelerated and Advance Payment Program and the impact it could have on future cash flows as the advances are repaid.
- ▶ Changes in the workforce.
- ▶ Governmental regulations that allow for expansion of services or the mandate to reduce services.
- ▶ Provisions in the CARES Act which allows for a five-year carryback for losses earned in 2018, 2019 and 2020, and the related cash flows from modifications of the related returns.
- ▶ The impact on investment markets, and the fact that anticipated returns are integral to an annual forecast (endowment spending).
- ▶ The impact on annual fundraising forecasts and the ability to achieve anticipated goals, for nonprofit healthcare entities.

Do we have to reassess our going concern position even if there was no prior history of substantial doubt of going concern?

Yes. ASC 205-40 requires that management evaluate an entity's ability to continue as a going concern for a period of 12 months from the date of issuance of the financial statements. Despite no prior history of substantial doubt of going concern prior to COVID-19, management must consider the facts, circumstances and impact that the pandemic may have on operations and the ability to service debt as it becomes due. Factors to consider include:

- ▶ Revisions to significant estimates such as allowances and valuations of inventory, which may impact future cash flows based on reductions in a consumer's ability to pay or a customer's need for supplies.
- ▶ The impact of COVID-19 on a market or geography that may be material to operations.
- ▶ Any SBA financing, as well as the likelihood of forgiveness and/or repayment.
- ▶ CARES Act Provider Relief Fund payments and the impact on cash flows.
- ▶ CMS Accelerated and Advance Payment Program and the impact it could have on future cash flows as the advances are repaid.
- ▶ Changes in the workforce.
- ▶ Governmental regulations that allow for expansion of services or the mandate to reduce services.

- ▶ Provisions in the CARES Act which allows for a five-year carryback for losses earned in 2018, 2019 and 2020, and the related cash flows from modifications of the related returns.
- ▶ The impact on investment markets, and the fact that anticipated returns are integral to an annual forecast (endowment spending).
- ▶ The impact on annual fundraising forecasts and the ability to achieve anticipated goals, for nonprofit healthcare entities.

## Debt

### How will we account for the amounts received from the Paycheck Protection Program (PPP)?

There are no specific U.S. GAAP standards on accounting by business entities for government assistance. Therefore, to determine the relevant accounting treatment, entities should analyze the nature and form of the assistance as well as the related conditions required to be met. This includes the Paycheck Protection Program (PPP).

Upon application, borrowers must certify in good faith that they were affected by the pandemic and that current economic uncertainty makes the PPP loan request necessary to support their ongoing operations. Borrowers are not required to demonstrate that they are unable to obtain credit elsewhere; however, the certification must consider the borrower's current business activity and its ability to access other resources of liquidity sufficient to support ongoing operations. As a safe harbor for SBA's review, loans with an original principal amount of less than \$2 million are deemed to have appropriately

made the required certification. This is because borrowers with loans below this threshold are generally less likely to have had access to adequate sources of liquidity in the current economic environment than borrowers that obtained larger loans.

The following guidance is included in U.S. GAAP:

- ▶ ASC 470 – guidance on accounting for debt
- ▶ ASC 740 – guidance about tax credits that are based on taxable income
- ▶ ASC 958-605, contribution accounting by not-for-profit entities. This guidance excludes from its scope transfers of assets from government to business entities.

PPP loans are not in the scope of ASC 740, Income Taxes or ASC 985-605, Not-for-Profit Entities—Revenue Recognition for business entities. In contrast to business entities, ASC 958-605 applies to government grants received by not-for-profit entities. Therefore, no analogy to IAS 20 would be made by NFPs.

As PPP loans are considered legal-form debt, it is appropriate to account for them as such under ASC 470, Debt. Under this model, the liability would only be derecognized upon repayment to the creditor or upon legal release under ASC 405-20, Extinguishments of Liabilities. In this context, we note that some entities may repay the PPP loan at the end of two years upon maturity, or earlier because they have reconsidered their eligibility. In those cases, debt accounting must be applied.

In contrast, other entities intend to apply for debt forgiveness. In that scenario, the entity could still elect to account for the PPP loan as debt pursuant to the guidance in ASC 470. However, legal release would only occur upon confirmation of forgiveness from the SBA under ASC 405-20-40-1(b).



Such forgiveness would be presented as a non-cash financing activity on the statement of cash flows. Further, interest imputation does not apply to this government loan program under ASC 835-30-15-3(e), even if the interest rate being charged is deemed to be below market.

Alternatively, it may be acceptable in limited circumstances to analogize to IAS 20, Accounting for Government Grants and Disclosure of Government Assistance. This analogy is only acceptable if:

1. The entity met the eligibility requirements to participate in the PPP, which may require legal analysis. As noted above, entities with loans under the \$2 million safe harbor may be eligible, absent evidence to the contrary.
2. At inception, it is probable the borrower will qualify for forgiveness. In practice, "probable" is commonly understood to mean 75% – 80% likely to occur.

Under an analogy to IAS 20, a deferred income liability would be recognized upon receipt of the forgivable loan if at the time of receiving the loan the entity has determined that it is probable that it would meet the conditions for forgiveness, i.e., the loan will be used to pay for qualifying salaries, rent, mortgage interest, and utilities. Similarly, no interest would be accrued due to the expectation of forgiveness.

The deferred income liability would be derecognized on a systematic basis over the periods in which the entity incurs the related expenses (e.g., payroll). That is, the deferred income would be recognized in the income statement as qualified expenses are paid and presented as either (1) other income or (2) a reduction of the related expenses. Presentation as revenue would not be appropriate. This approach will result in the recognition of the proceeds as a grant for the amount expected to be forgiven prior to legal release; the remainder (if any) would be recognized as a loan consistent with ASC 470 and derecognized upon repayment or legal release in accordance with ASC 405-20.

## Debt Covenants

### How should we address potential debt covenant issues or violations?

Every organization should forecast the impact of the pandemic on their current and future operations. If an organization determines there is uncertainty around complying with debt covenants, the most prudent recommendation would be to contact their lender to understand their position on covenants during this uncertain economic time. Organizations should start a dialogue with their lenders around potential waivers

and what the lenders are doing to assist their clients during this time.

If a covenant violation occurs after the balance sheet date but before the financial statements are issued, a current classification may be required unless the entity obtains a waiver before the financial statements are issued. Thus, the lender is not able to require repayment for more than one year after the balance sheet date. If you must delay the issuance of Dec. 31, 2019 financial statements, these scenarios may become more frequent.

### Do we move outstanding debt amounts to current if we are uncertain at this time if we will meet the covenants?

The movement of outstanding debt amounts to current should not be done until an organization has undergone an extensive forecasting exercise and discussed that forecasting with their independent auditor and lending institution.

If a covenant violation has not occurred prior to issuance, but it is probable the entity will violate a covenant within a year of the balance sheet date, judgment will be required to determine the appropriate classification. Entities are encouraged to consult with their advisers in these situations.

## Debt Restructuring

### If we restructure debt, what are the tax and accounting implications?

As entities work with lenders to address these potential issues, terms of debt arrangements may be modified to address covenant violations, or payment terms may be changed to alleviate cash flow burdens in the near-term. Entities may wish to conduct these lender negotiations considering the going concern assessment period, which is typically one year after the financial statements are issued (as opposed to one year after the balance sheet date). Entities will also need to consider whether modifications are troubled debt restructurings. If they are not troubled debt restructurings, further analysis on whether the changes in terms should be accounted for as a modification or as an extinguishment will be required.

As entities work with lenders to modify or extend the payment terms of debt arrangements, they must also be cognizant of the potential tax implications of debt modifications. In instances where there is an exchange of old debt for new debt, the exchange may be treated as a taxable event creating taxable income for the obligor. The ultimate tax effect of debt modifications can depend on the debtor's status with

respect to bankruptcy or insolvency, its history of available net operating losses and its continuing operations. Entities should consider all elements of a restructuring, including its impact on future years' taxable income prior to undertaking a significant modification process.

## Fair Value Measurement

### How do current market conditions impact fair value measurements?

There are many areas of U.S. GAAP that require the use of a fair value measurement. ASC 820, *Fair Value Measurement* defines fair value as the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date. One of the key concepts in that definition is an orderly transaction, which is designed to differentiate between what is considered a fair value measurement vs. a distressed sale or a forced transaction.

Current market conditions are under extreme stress and may produce values that an entity may wish to disregard; however, it would only be appropriate to disregard market observable values or inputs to a fair value measurement if they were based on transactions that were not 'orderly' transactions. In addition, recent events are likely to impact credit risk in fair value measurements. This could affect a counterparty's ability to pay under receivable and derivative contracts, as well as the entity's own risk of nonperformance (e.g., if the entity reports its own debt at fair value).

## Investments

### Can we disclose our portfolio decline in debt securities as temporary, given the uncertainty of the situation?

ASC 320, *Debt Securities* (prior to adoption of ASU 2016-13) lists steps for identifying and accounting for impairments of Available-for-Sale or held to maturity debt securities and notes that a determination will need to be made for temporary or other-than-temporary decline. Steps include:

- ▶ Step 1: Determine whether an investment is impaired, which is defined in FASB ASC 320-35-21 as "fair value of the investment is less than its cost."
  - Factors for impairment are:
    - Significant deterioration
    - Change in regulatory environment
    - Change in general market conditions amongst others.

- ▶ Step 2 (ASC 320-10-35-29): Evaluate whether an impairment is other-than-temporary—daily large swings within the market would not defer to other than temporary. ASC 320-35-33 notes that "questions sometimes arise about whether an entity shall recognize an 'other-than-temporary' impairment only when it intends to sell a specifically identified available-for-sale equity security at a loss shortly after the balance sheet date. When an entity has decided to sell an impaired available-for-sale security and the entity does not expect the fair value of the security to fully recover before the expected time of sale, the security shall be deemed other-than-temporarily impaired in the period in which the decision to sell is made, not in the period in which the sale occurs."
- ▶ If it is determined in Step 2 that the impairment is not temporary, then an impairment loss shall be recognized in earnings equal to the entire difference between the investment's cost and its fair value at the balance sheet date of the reporting period for which the assessment is made. (ASC 320-10-35-34)

## Lease Accounting

### How do we account for rental holidays and abatements that we have negotiated with our landlords due to the closure of our offices during COVID-19?

Because of the disruption caused by COVID-19, it is expected that many landlords will provide (or that many lessees will request) rent concessions. Landlords may be offering concessions to lessees in the form of free (or reduced) rent, deferral of rent payments interest free, or cash payments when operations of the lessee are interrupted or are significantly affected by COVID-19. Whether a landlord concession is a modification or a concession in accordance with the original lease depends on the enforceable rights and obligations of the lessee and lessor in the lease contract (e.g., based on a force majeure or similar provision) and of the jurisdiction in which the lease contract is governed, and such evaluation may require legal assistance. If a lessee in response to COVID-19 does not pay rent when due (or only pays a portion of the rent otherwise due), lessee's and lessor's accounting generally should not change until the parties approve changes to the rent payments unless such absence (or reduction) of rent payment is contemplated in the original lease contract. The potential large volume of contracts to be assessed under either ASC 842 or ASC 840 may be particularly burdensome, complex, and challenging for many entities to determine whether each lease contract provides enforceable rights and obligations related to those lease concessions.



Landlord concessions that are considered modifications under ASC 842 typically will be accounted for as a modification of the original lease (i.e., not as a separate contract) because the modification will not grant the lessee any additional right of use. The modification of an existing lease will require the lessee to remeasure and reallocate the remaining consideration in the contract, reassess lease classification, update the discount rate, and remeasure the lease liability and the carrying amount of the right-of-use asset. A lessor will make a similar determination to account for a lease modification as a modification of the existing lease and make appropriate changes to remeasure amounts recorded. Lease terminations (full or partial) will also need to be accounted for by the lessee and the lessor in accordance with ASC 842. ASC 840 has its own lease modification guidance, which is substantially different from that in ASC 842.

At its April 8, 2020 Board meeting, the FASB staff discussed a technical inquiry it received related to rent concessions; specifically, whether concessions related to the effect of COVID-19 are required to be accounted for in accordance with the lease modification guidance in ASC 842 or ASC 840. At that meeting, the FASB staff noted that the lease modification guidance in ASC 840 and ASC 842 contemplates routine changes in terms and conditions of lease contracts negotiated between lessees and lessors, but not changes rapidly executed on a global scale that arise as a result of COVID-19. Accordingly, the FASB staff stated that for concessions related to COVID-19, an entity could decide not to analyze each lease contract to determine whether enforceable rights and obligations for concessions exist. Instead, an entity can elect to account for lease concessions related to the effects of COVID-19 as if those concessions arise from the enforceable rights and obligations of the existing contract (regardless of whether those concessions explicitly exist in the contract). The election can be made for concessions if the total cash flows required by the modified contract remain substantially the same or are less than the total cash flows before the concession. The FASB staff expects that reasonable judgment will be applied in that determination.

### How should the cost of exiting a lease be treated?

ASC 842-20-40-1, *Lease Accounting*, notes that a termination of a lease before the expiration of the lease term shall be accounted for by removing the right of use asset and the related lease liability with a profit or loss recognized for the difference. Any termination penalties should be included in the profit or loss calculation. For lessors, if the lease has been classified as either a sales-type or a direct financing lease, a lessor shall test the net investment in the lease (the sum of the remaining lease receivable and the unguaranteed residual value of the asset) for impairment and recognize any impairment loss identified. The remaining net investment in the lease shall be reclassified to the appropriate asset category and accounted for under the guidance provided for that asset category.

ASC 840-30-40-1, *Lease Accounting*, notes that a termination of a capital lease before the expiration of the lease term shall be accounted for by the lessee by removing the asset and obligation, with a gain or loss recognized for the difference. Termination of a capital lease for a lessor shall be accounted for by removing the net investment in the lease and recording the leased asset at the lower of its original cost, present value or present carrying amount. The difference should be recorded as a profit or loss in the period of termination.

### I am going to default on my lease, what are the accounting implications?

Review the terms of the lease to ensure that it can be modified, cancelled or terminated early. ASC 842, *Lease Accounting*, defines the “lease term” as the noncancelable period during which the lessee has the right to use the underlying asset, adjusted for any extension or termination options that the lessee is reasonably certain to exercise, as well as any options to extend or terminate the lease that is controlled by the lessor. The lease term includes free rent periods and begins at the commencement date of the lease. (See ASC 842-10-30-1).

A lease may specify a penalty that must be paid if the lessee terminates the lease early. ASC 842-20-40-1 notes the termination of a lease before expiration of the term shall be accounted for by removing the right of use asset and the related lease liability, with profit or loss recognized for the difference. Any termination should be included in the profit or loss calculation.

Lessees should monitor whether there are any indications of right-of-use asset impairment. Right-of-use assets are tested by lessees for impairment in accordance with ASC 360-10. Even if a right-of-use asset is not impaired, a lessee may have to reassess (shorten) the useful life of the asset as appropriate (for example, when the right-of-use asset is part of a larger asset group that is not impaired, but the entity plans on abandoning the lease before the end of the initial lease term). In the current environment, lessees should exercise care in monitoring and timely identifying triggering events requiring impairment testing and reassessment of useful lives. Also, while charges that are considered lease payments (whether fixed or variable) are excluded from the guidance in ASC 420 on exit or disposal cost obligations, if the lease contract includes non-lease components and the lessee elected to separate the lease and non-lease components, the lessee should accrue the portion of fixed payments and estimated variable payments allocated to the non-lease components on the cease-use date of the underlying asset.

## Telehealth

### How do I set up appropriate accounting for telehealth revenues and services?

There are many different telehealth revenue models, but organizations must consider all under ASC 606, if your company has adopted it. Otherwise the revenue accounting would have to be considered under previous revenue guidance, specifically ASC 605, *Revenue Recognition*.

A common telehealth model would be where an organization that provides telehealth services enters into a contract with clients who purchase access to the organization's professional provider network. This includes physicians or other clinicians for their members, their dependents and other beneficiaries. The organization's contracts with its clients include per-member-per-month subscription access fees as well as additional specific revenues that are generated on a per telehealth visit basis for specialty medical services. These contracts usually have a duration of one year or less.

Revenues are recognized when the organization satisfies its performance obligation to stand ready to provide

telehealth services which occurs when the organization's clients and members have access to and obtain control of telehealth services.

Revenue is recognized in an amount that reflects the consideration that is expected in exchange for the service and includes a variable transaction price as the number of members may vary from period to period.

Often, these contracts include performance guarantees based upon minimum member utilization and guarantees the organization for a specific level of performance of its services. If guarantees are not being realized, the organization will record a reduction to revenue, as estimates of the amount that will be due at the end of the respective client's contractual period.

### How do I ensure our new telehealth services are compliant with HIPAA and other laws?

For healthcare providers that are providing telehealth services from home, it's critical to review and ensure the patient information protection of any apps or communications platforms in use.

Healthcare organizations must also equip their employees with the knowledge and tools necessary to maintain proper security protocols and protections when working from home. Some employees, for example, may not be as comfortable in their technology skills and struggle to adjust to processes in place to maintain security.

Steps like training each employee on best practices for secure remote work; providing HIPAA rules updates; reviewing data regulations and making relevant information available to employees; and maintaining clear and consistent communication to employees on changing regulations, evolving vulnerabilities and any other concerns as they arise are important steps.

As HIPAA stands today, the extent to which covered entities can or cannot disclose protected health information to organizations beyond the traditional care continuum to coordinate patient care is unclear. However, HHS allows providers to share patient information to assist in nationwide public health emergencies and in making sure patients receive the care they need.

To navigate a changing risk environment around patient privacy during this time, providers must continue to:

- ▶ Review temporary COVID-19-related healthcare guidelines from government agencies

- ▶ Reinforce policies and procedures that protect protected health information against impermissible uses and disclosures
- ▶ Be diligent in scrubbing personal identification information from patient data and in determining what information, if any, is necessary to disclose
- ▶ Limit exposure to cyber threats and bad actors as telehealth capabilities expand to meet patient need and curb nonessential visits to the hospital
- ▶ Address and comply with data privacy and cybersecurity requirements as they introduce new technology solutions to meet changing public health demands

## Business Combinations

[We were completing an acquisition of a business on Dec. 31, 2019. How do we factor in the impact of COVID-19 in our projections to determine the value of intangibles in our purchase price allocation accounting under ASC 805, Business Combinations?](#)

Projections for analyses completed as of Dec. 31, 2019 should not include the impact of COVID-19. Valuations rely on several company specific market factors, so it is important that those assumptions be isolated to represent value as of a single (date) point in time. Because of that, valuations should be performed only using information that was known or knowable as of the date of valuation. As of year-end 2019, we were aware that China had identified individuals that had contracted the coronavirus (not yet named at the time), but we had no way of knowing that it would become so widespread across the globe. Nor did we then, or even still, understand the significant impact it would have on our lives and the economy.

The WHO officially classified COVID-19 as a global pandemic on March 12, 2020. That's when we consider it to be known and knowable for valuations from a global perspective including most of the U.S. The timing may vary a bit if a company's primary operations or customers are in a country that was impacted earlier in 2020, but not prior to that.

## Goodwill Impairment Analysis

[When should a goodwill impairment analysis be completed? How frequent should assessments of impairment occur?](#)

ASC 350-20, *Intangibles – Goodwill and Other* – notes that goodwill (except goodwill that is being amortized under the private company election) must be tested annually for impairment. Annual goodwill impairment tests may be performed any time during the fiscal year provided the test is performed at the same time every year. Different reporting units may be tested for impairment at different times. Entities should evaluate their own facts and circumstances in assessing whether to establish different reporting dates for different reporting units.

ASC 350-20-35-30 specifies that goodwill of a reporting unit shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. Paragraphs 350-20-35-3C(a) through (g) include examples of such events and circumstances. Annual testing for goodwill impairment notwithstanding, management must remain aware of events or circumstances that could indicate that a potential impairment has occurred between prescribed annual testing dates and must respond accordingly to such events or circumstances.



For questions specific to your organization, reach out:

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