


Navigating the Covid-19 Unnatural Disaster

December 7, 2020

As 2020 Opened ... the Taste of a New World

Zero Rates, If a Response to the Shock, Are No Antidote for Equities ...

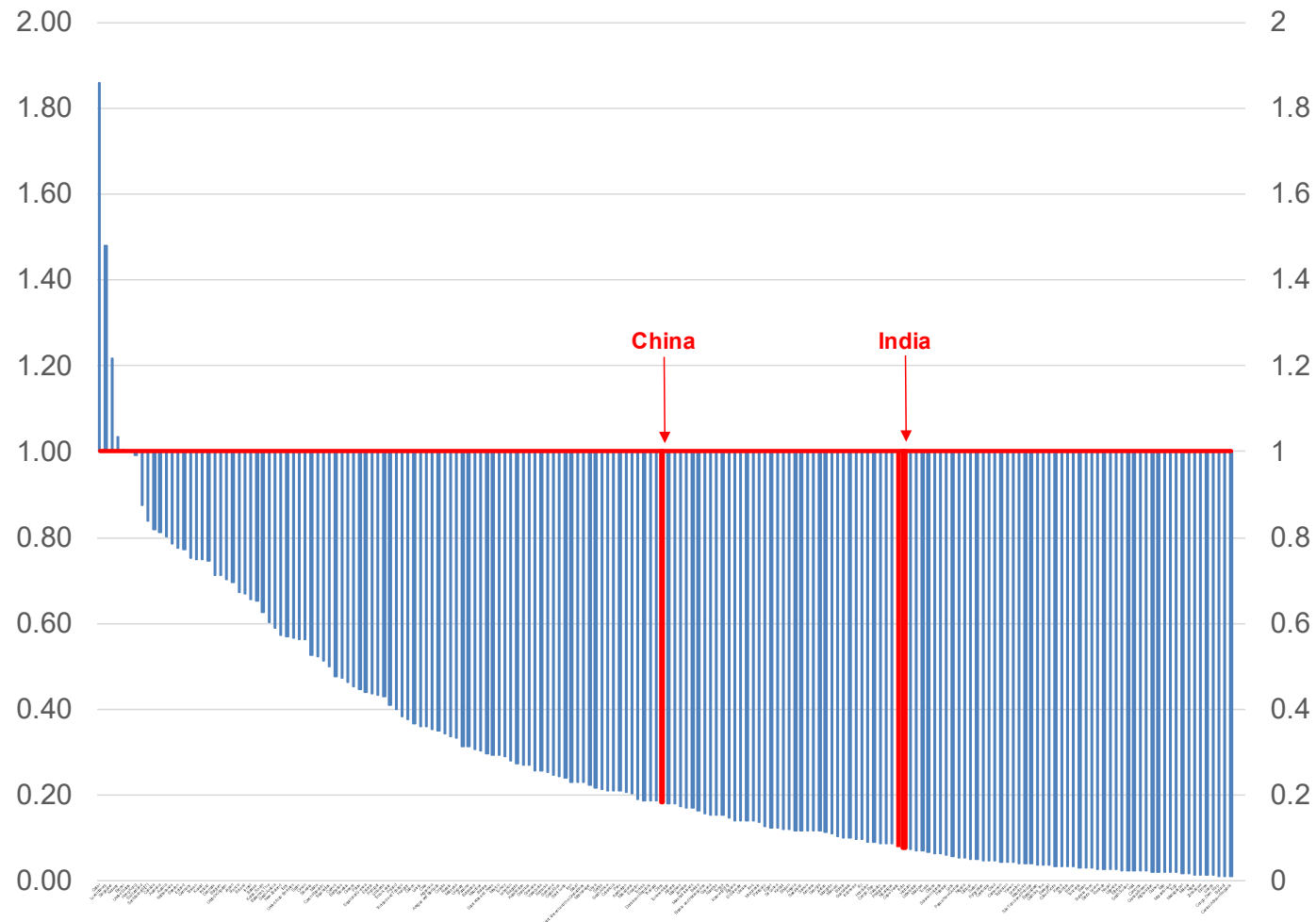
- If rates have been very low for a while;
- If economic upheaval is the reason for low rates.

Favorable Structural Themes on Three Fronts ...

- (1) Cyclical dynamic of the U.S. economy points to a higher noninflationary operating rate ('high pressure economy') and less business cycle risks;
- (2) Innovation is transforming the economy and, because it is disruptive, is the force behind the growing income divide;
- (3) Trade spats put the spotlight on an emerging source of new economic energy, new economic opportunity, and new competition and only underscore who is in the driver's seat—economics and not politics.

People In Motion ... All Across the Ocean

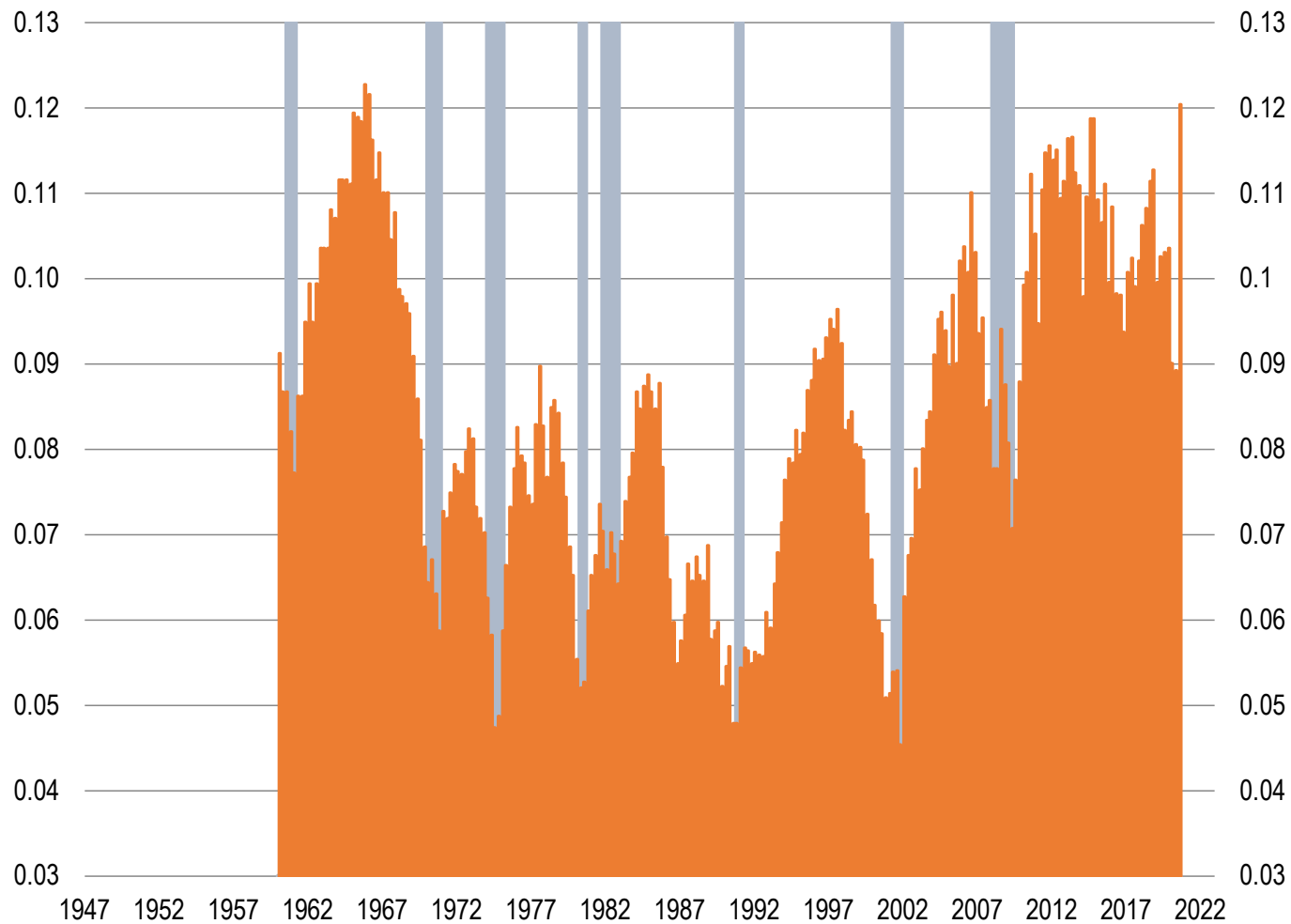
Relative real GDP per capita (ratio to U.S. real GDP per capita, 2016 dollars)



Sources: Haver Analytics; CIA. Updated through 2019 Q2.

Record Business Performance ...

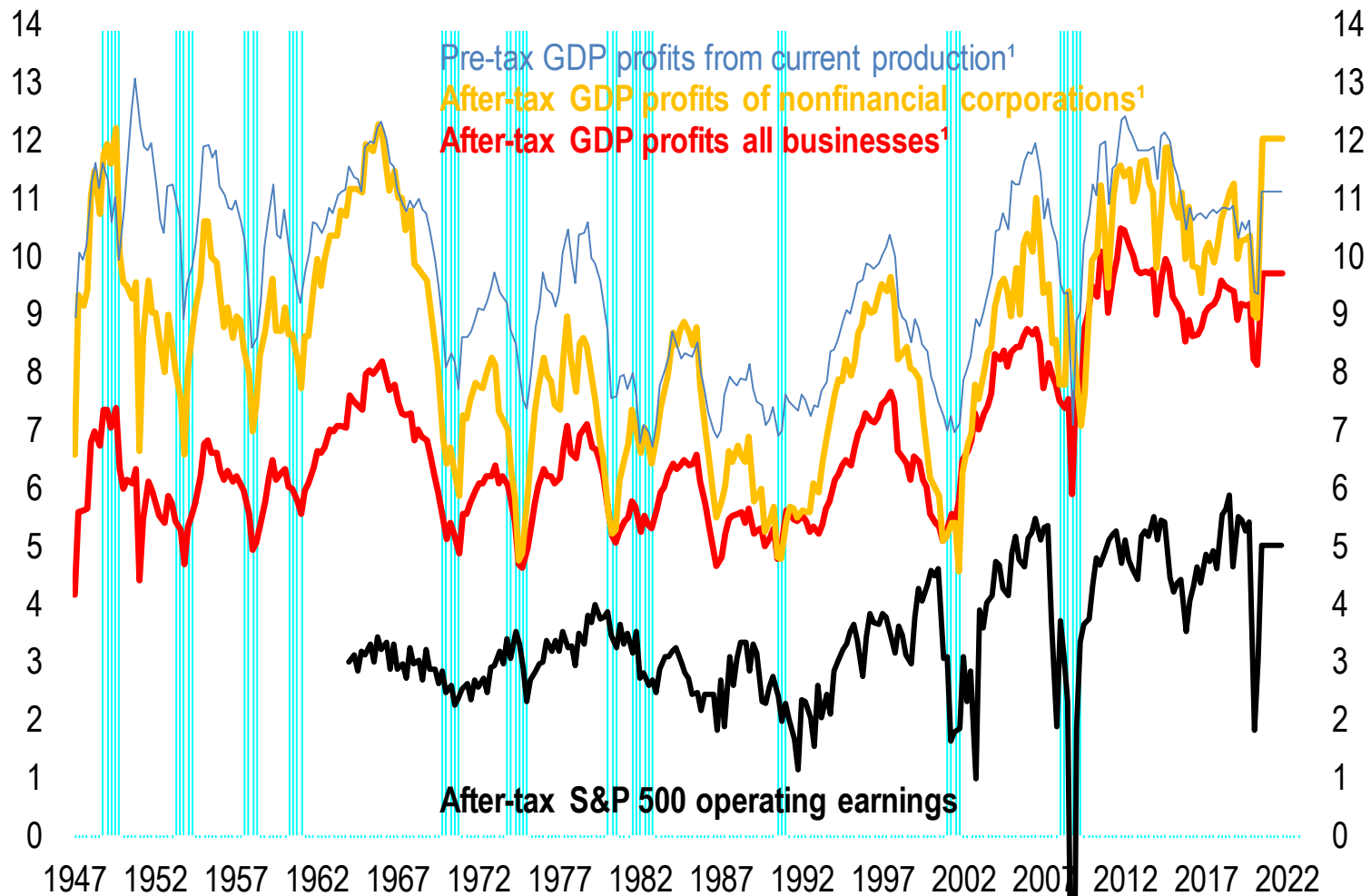
After-tax profits of nonfinancial corporations (percent of the sector's value added)



Sources: Haver Analytics; U.S. Department of Commerce. Updated through 2020 Q3.

... Challenges the “Cyclical Reversion” Idea

Selected measures of business profits (percent of Gross Domestic Income)

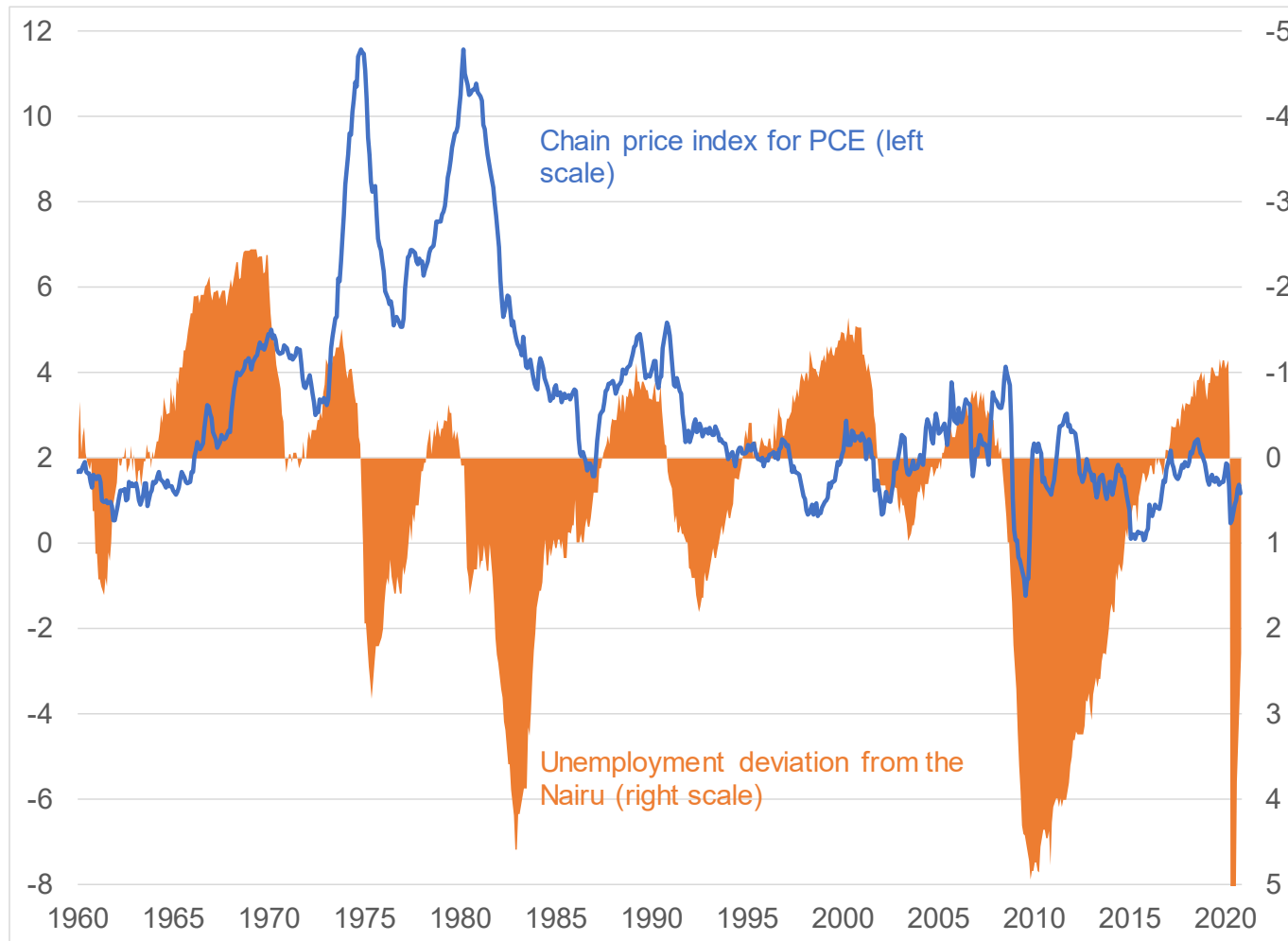


Sources: Haver Analytics; U.S. Department of Commerce. Updated through 2020 Q3.

3.5% Unemployment, Stable Inflation?!

Chain price index for PCD (% oya)

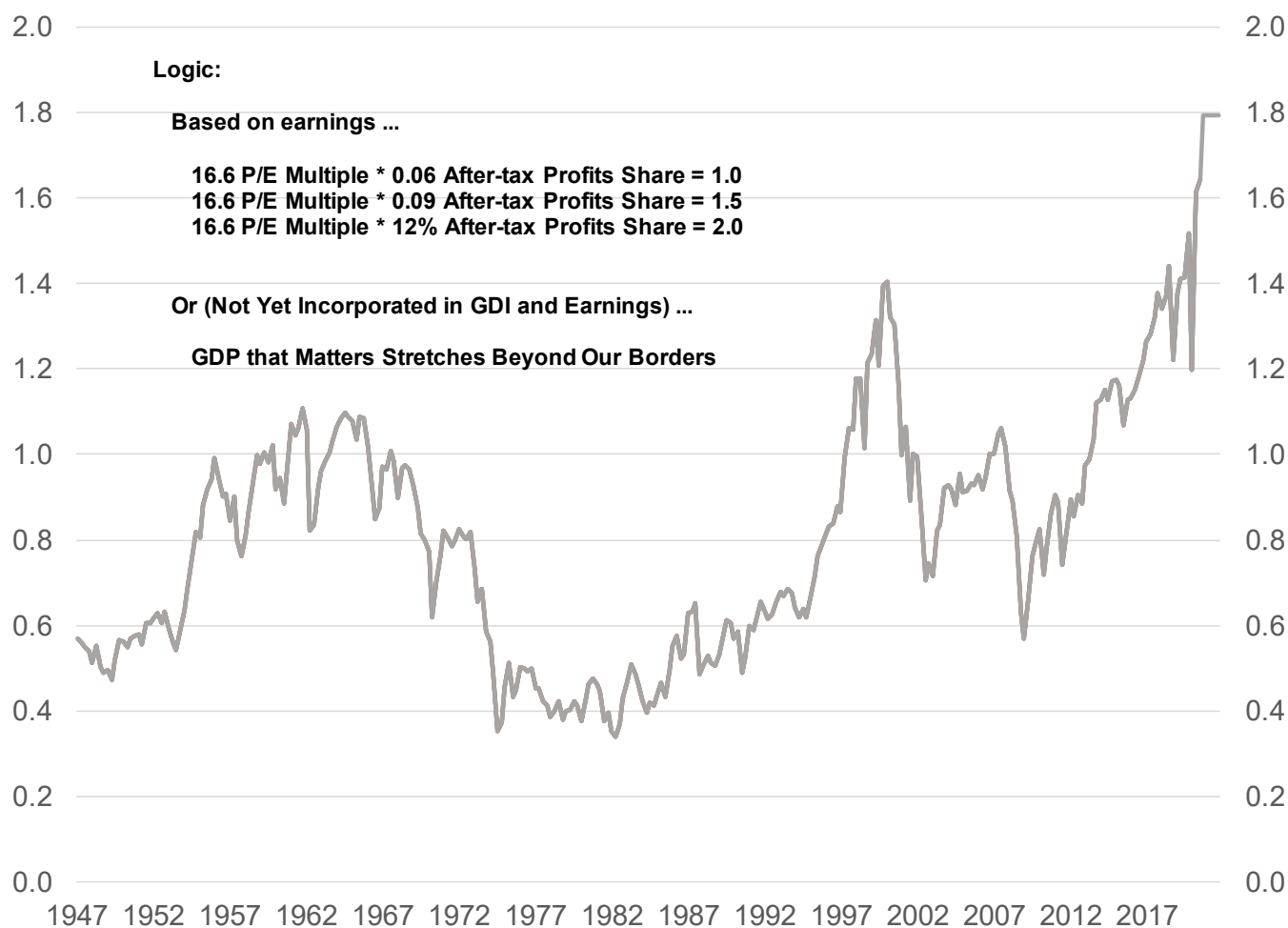
Unemployment deviation (U – U natural rate, pct pts)



Sources: Haver Analytics; U.S. Department of Commerce; U.S. Department of Labor. Updated through October 2020.

Themes Accentuated by Covid-19

Ratio of the value of the U.S. stock market to Gross Domestic Income



Sources: Haver Analytics; Federal Reserve Board; U.S. Department of Commerce. Updated through 2020 Q3 (GDI) and December 4, 2020 (equities).

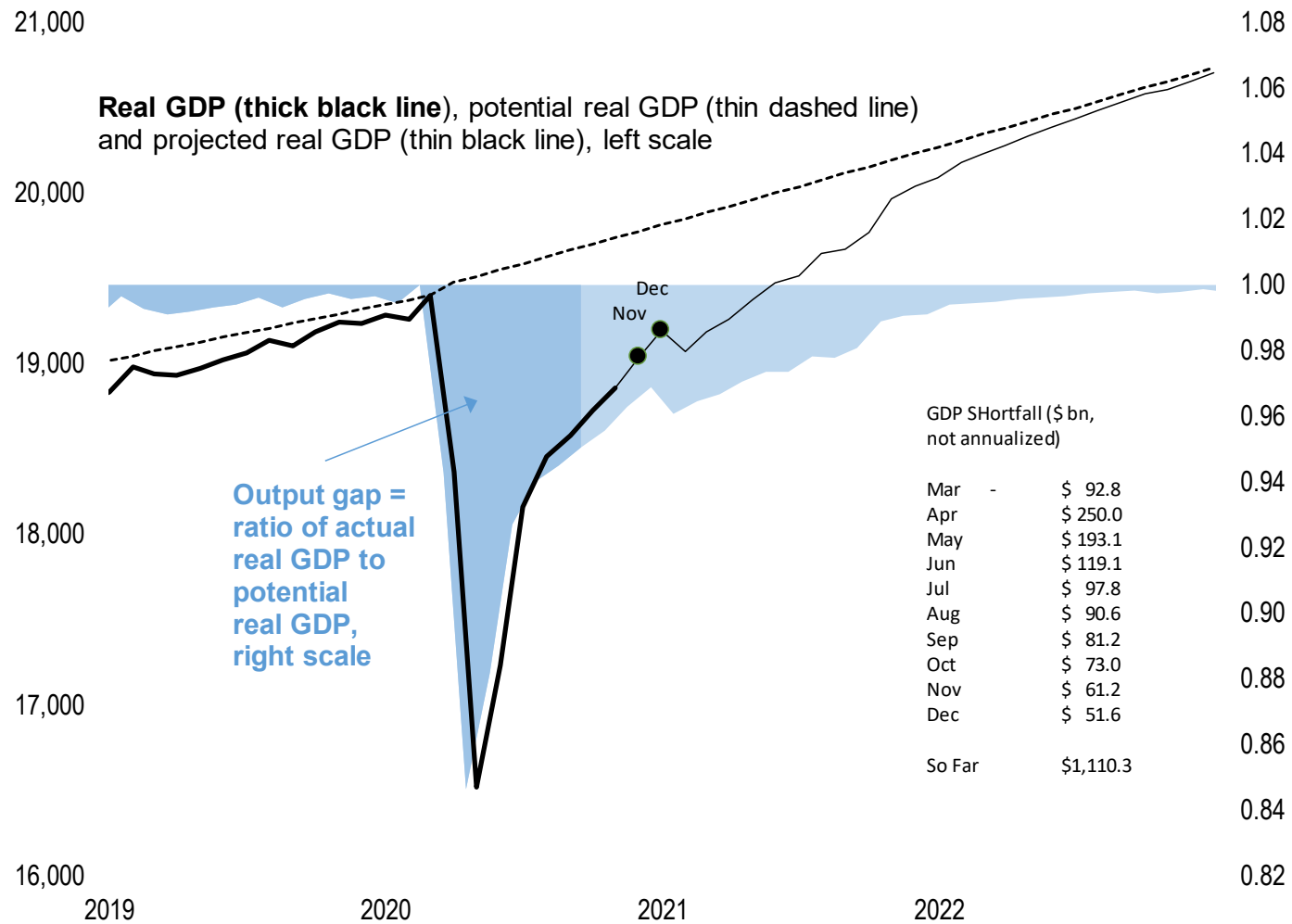
Why the Visibility Beyond Covid Is So Clear

Investors Require Little Imagination, Because ...

- (1) We knew medical science was working at Warp Speed and in new frontiers;
- (2) Years of technological innovation eased the shift to remote working and shopping and the digital arena offers greater business efficiency;
- (3) An unprecedented policy response (known by the evening of March 27, before the ink was dry on the CARES Act) seemed likely to get furloughed workers and many small businesses over the lockdown hurdles.

GDP Progress Report

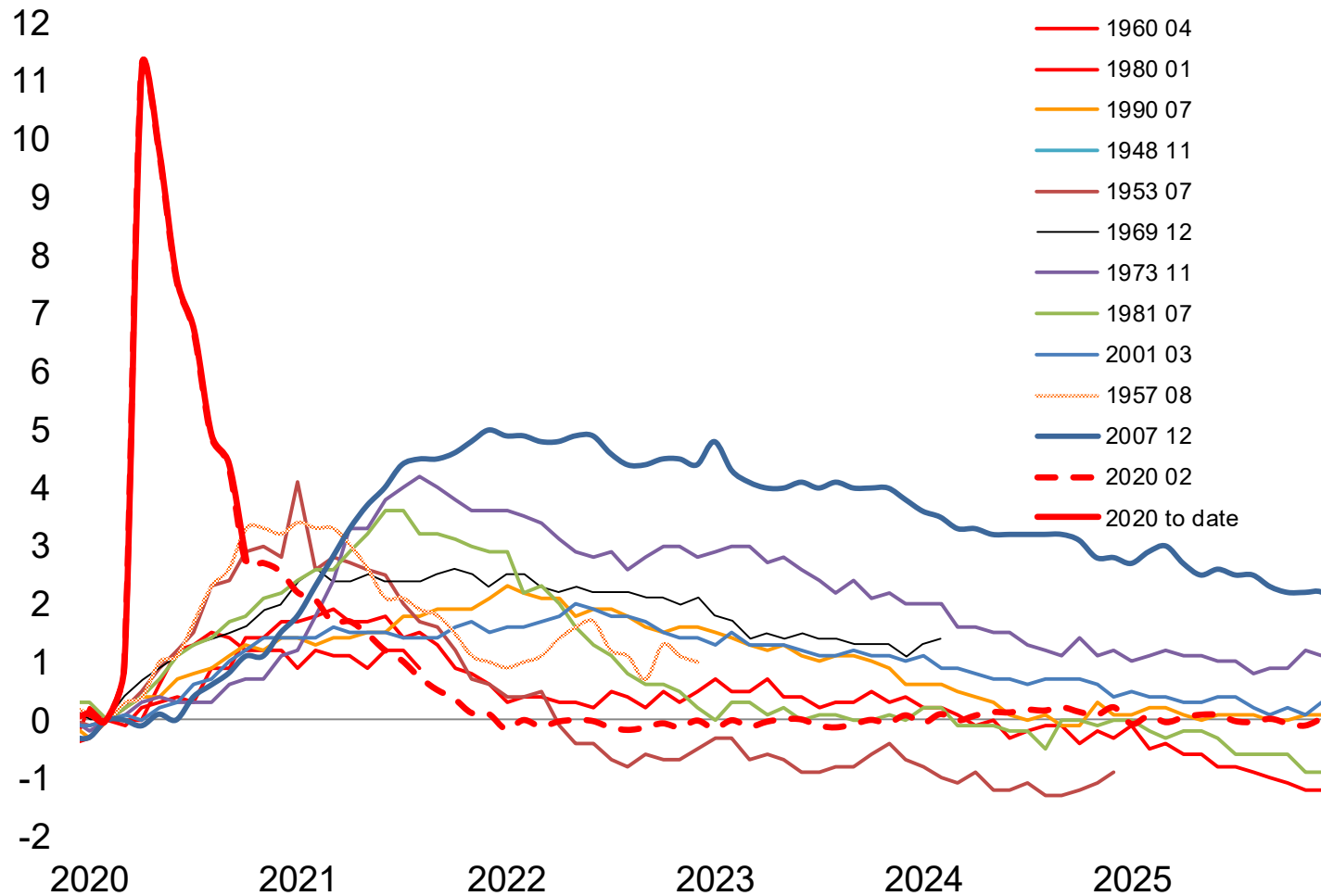
Real GDP (billions of chained 2012 dollars)



Sources: Haver Analytics; IHS Market. Updated through October 2020.

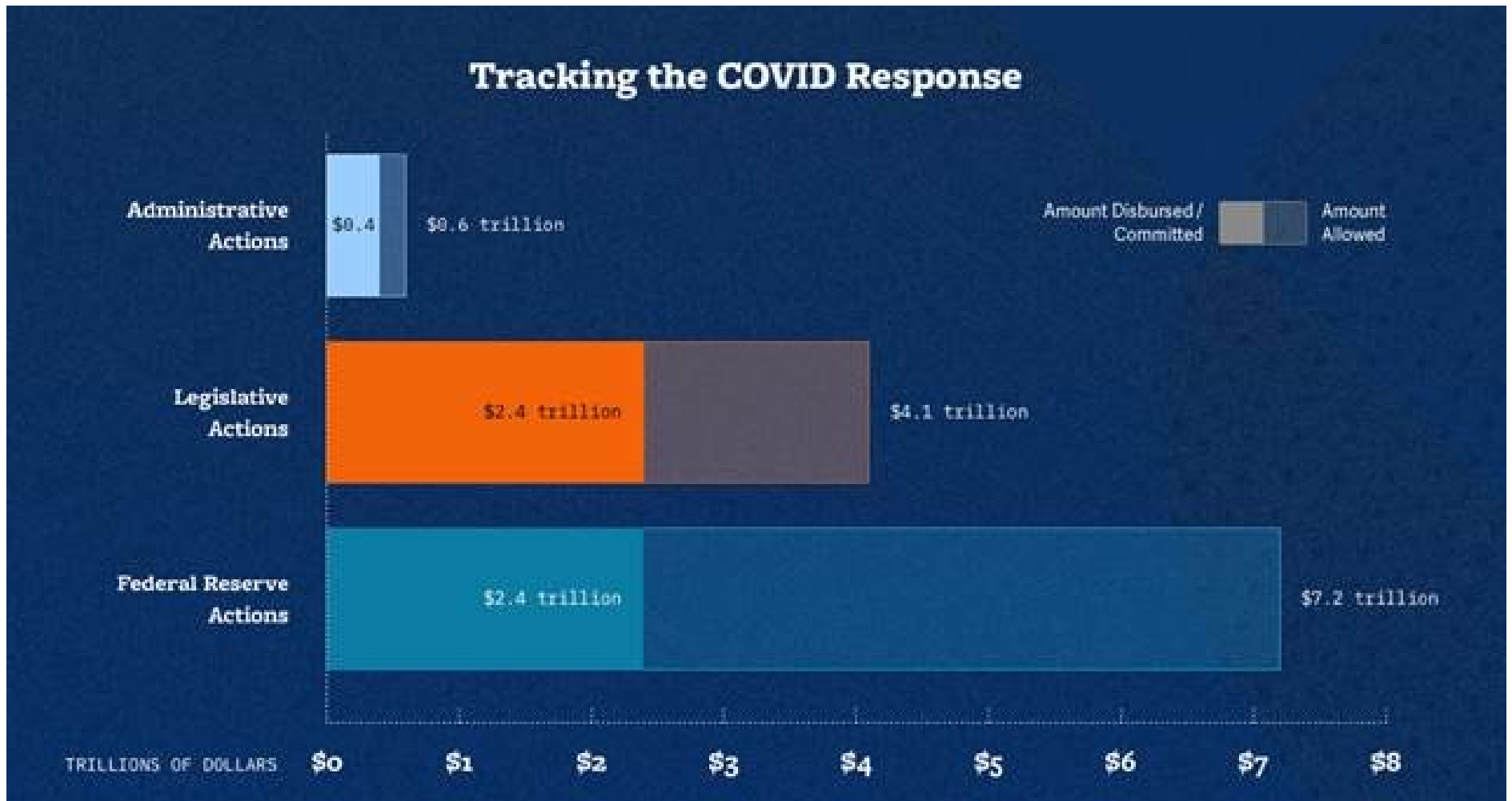
The Lockdown Shock Is No Rerun

Deviation of the unemployment rate from the business cycle low point (percentage points)



Note: The unemployment low point of each cycle is lined up to February 2020.
Sources: Haver Analytics; U.S. Department of Labor. Updated through September 2020.

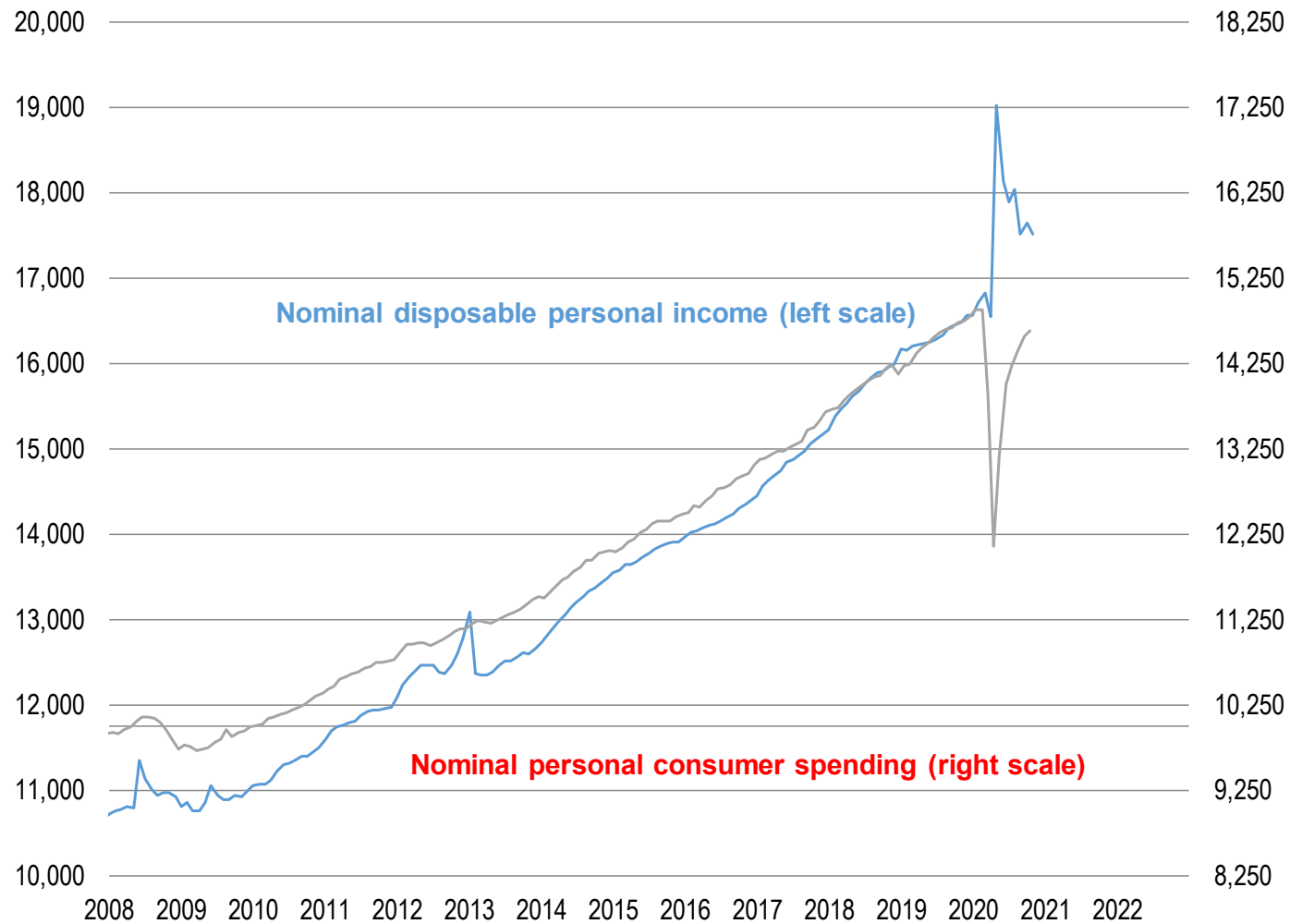
\$4.7 trillion Aid, Kind of Unprecedented ...



Source: Center for a Responsible Federal Budget. Updated through November 23, 2020.

Have Income ...

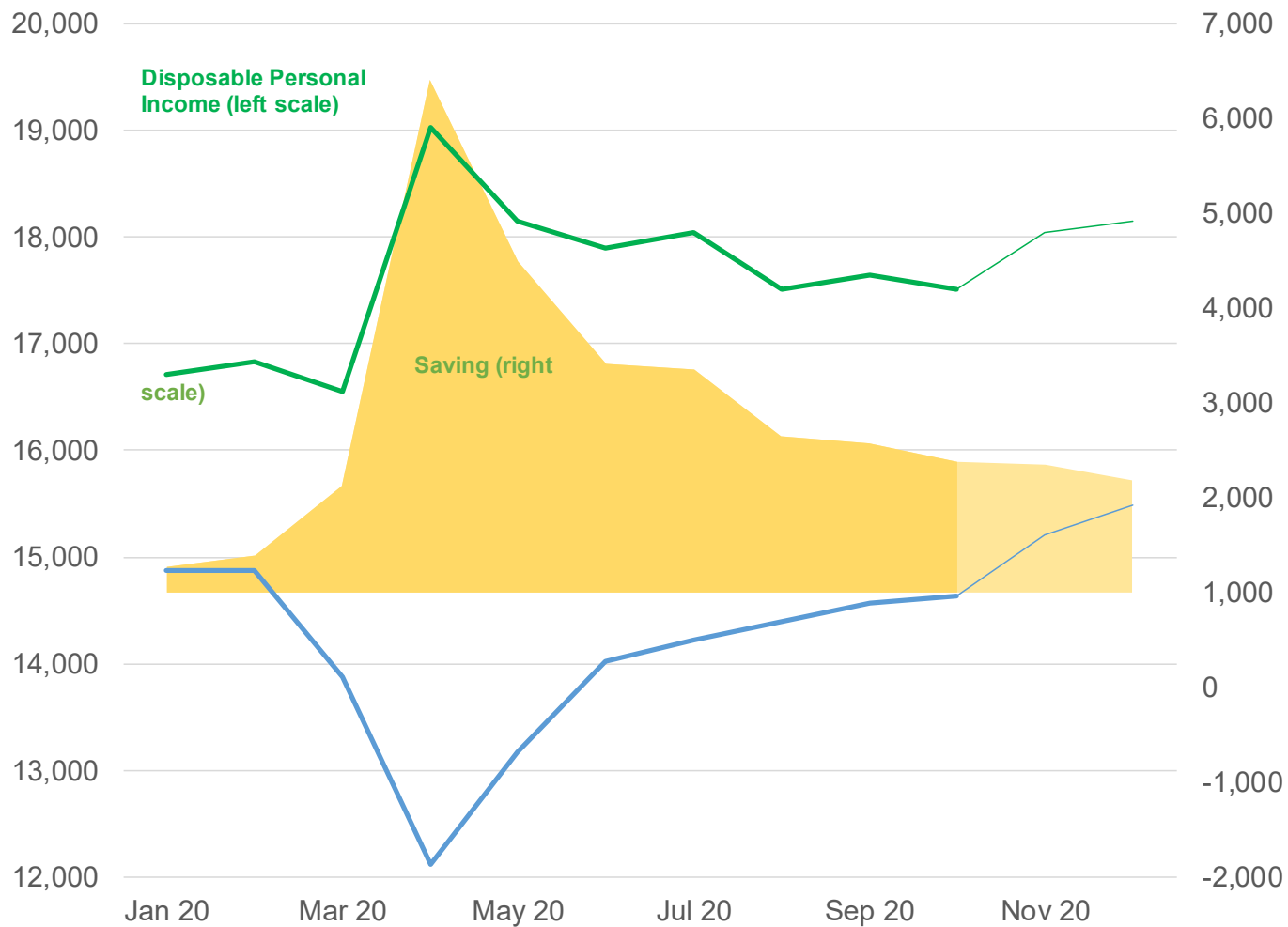
Income, Spending and Saving (billions of dollars annualized)



Sources: Haver Analytics; U.S. Department of Commerce. Updated through October 2020.

... Have Saving

Income, Spending and Saving (billions of dollars annualized)

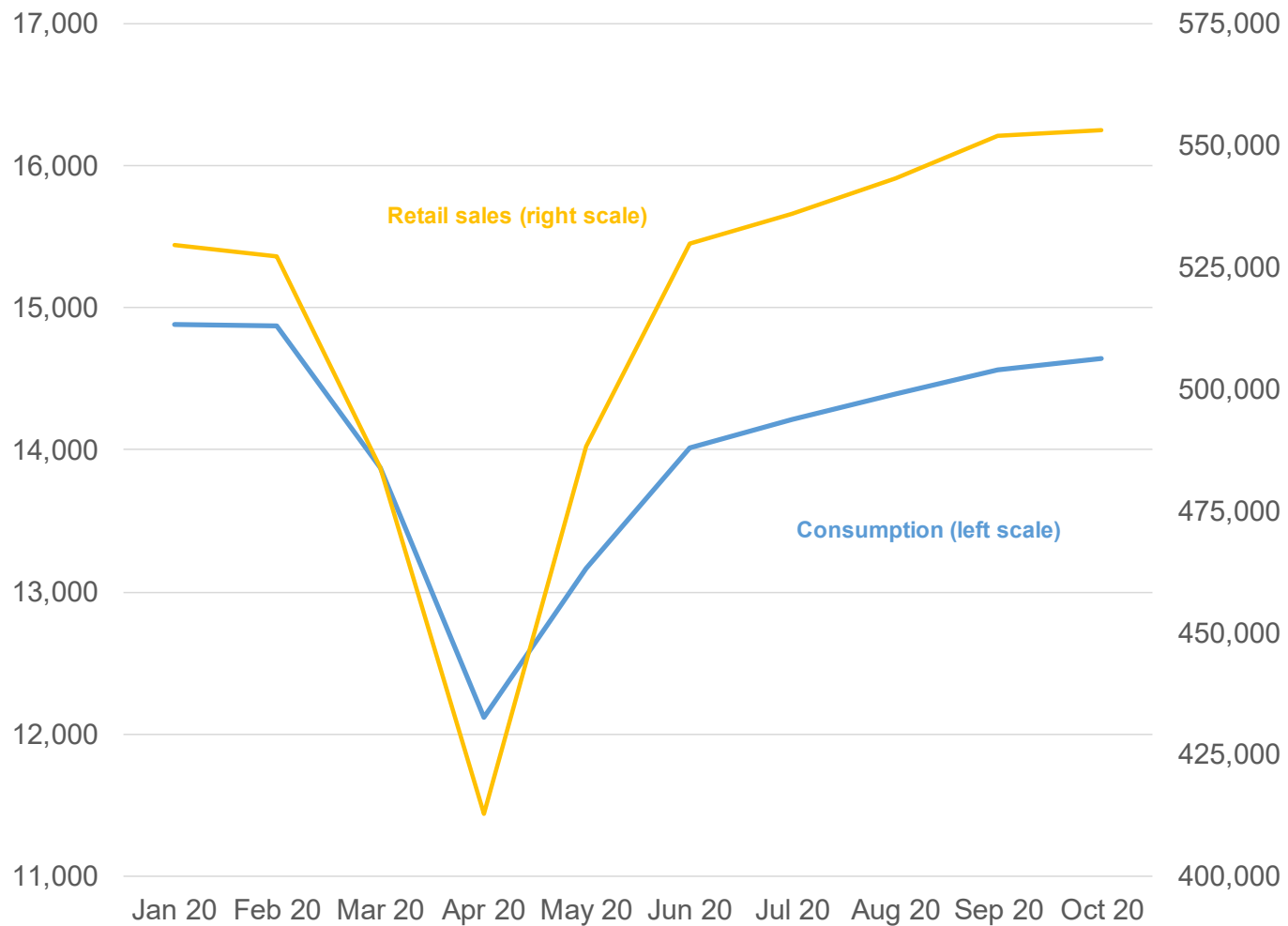


Sources: Haver Analytics; U.S. Department of Commerce. Updated through October 2020.

... Will Spend

Nominal consumer spending (billions of dollars)

Retail sales (millions of dollars)

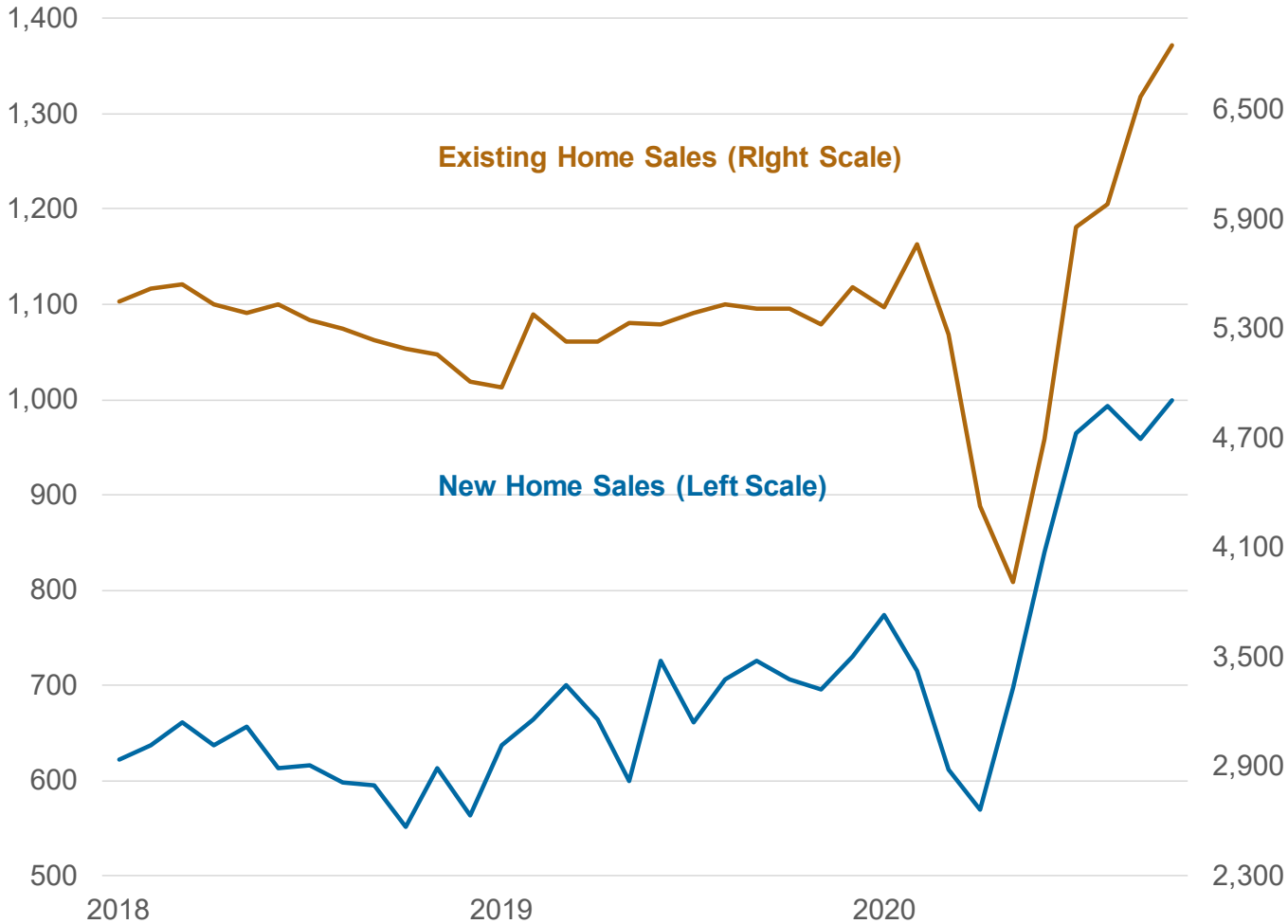


Sources: Haver Analytics; Census; Bureau of Economic Analysis. Updated through October 2020.

I'm Guessing You're Frenzied

New home sales (thousands annualized)

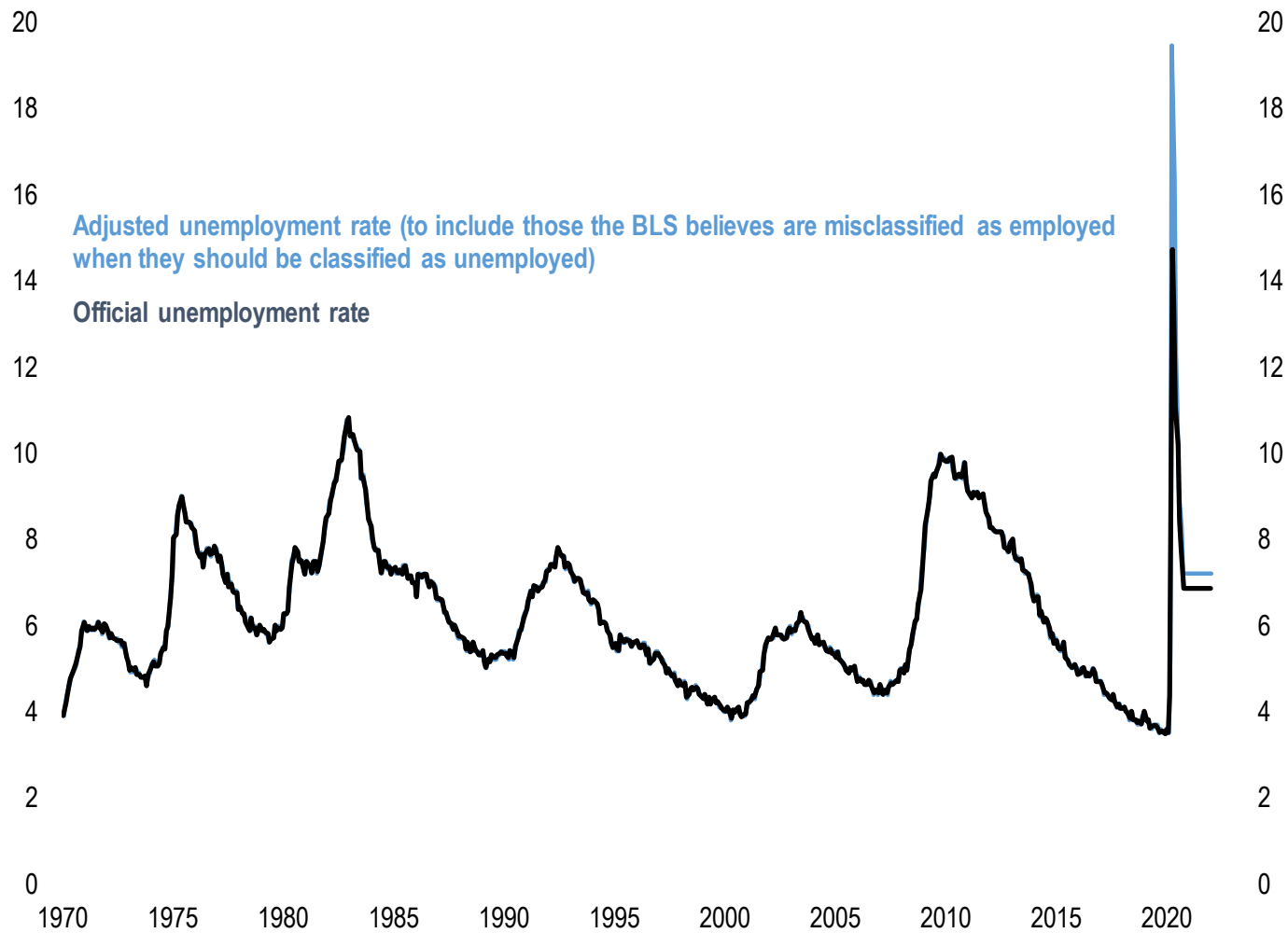
Existing home sales (thousands annualized)



Sources: Haver Analytics; Census; National Association of Realtors. Updated through October 2020 (new home sales) and October 2020 (existing home sales).

And It Did This

Unemployment (percent of the labor force)



Sources: Haver Analytics; U.S. Department of Labor. Updated through October 2020.

UI Flows Know the Deal

Insured unemployment programs (thousands)

| Sharing (NSA, Number) | Weekly Unemployment Insurance Flows | | | | | | | | | BLS Monthly Survey | | |
|--|-------------------------------------|--------|--------|-------|--------|-------------|--------------|--------------|--------------|--------------------|--------|--------|
| | 17-Oct | 24-Oct | 31-Oct | 7-Nov | 14-Nov | 21-Nov | 28-Nov | 5-Dec | 12-Dec | Sep | Oct | Nov |
| <i>Figures are weekly or monthly changes in thousands</i> | | | | | | | | | | | | |
| Net Change in Recipients of Regular Benefits (Claimants) | -649 | -601 | -424 | -428 | -281 | -569 | -500 | -500 | -500 | -1,745 | -4,924 | -1,734 |
| Initial Applications for Regular Benefits (Jobless Claims) | 797 | 758 | 757 | 711 | 748 | 787 | 712 | 712 | 712 | 3,654 | 4,128 | 2,974 |
| Implied Outflow from Regular Programs | 1,446 | 1,359 | 1,181 | 1,139 | 1,029 | 1,356 | 1,212 | 1,212 | 1,212 | 5,399 | 9,052 | 4,708 |
| Change in the Number Receiving Additional Benefits From: | | | | | | | | | | | | |
| PEUC | 273 | 160 | 233 | 132 | 60 | 50 | 50 | 50 | 50 | 451 | 2,151 | 585 |
| Extended Benefits | 172 | -17 | 78 | -33 | 80 | -30 | 80 | -30 | 80 | 100 | 305 | 108 |
| State Extended Benefits Programs | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 305 | 108 |
| PUA | -1,290 | 101 | -751 | 527 | -339 | 500 | -300 | 500 | -300 | -1,688 | -2,821 | -463 |
| Change in Selected Populations Receiving Unemployment Insurance Benefits | | | | | | | | | | | | |
| Regular + PEUC | -376 | -441 | -191 | -296 | -221 | -519 | -450 | -450 | -450 | -1,558 | -2,773 | -1,149 |
| Regular + PEUC + EB | -204 | -459 | -112 | -328 | -142 | -549 | -370 | -480 | -370 | -1,369 | -2,469 | -1,040 |
| Regular + PEUC + EB + State EB | -204 | -459 | -112 | -328 | -142 | -549 | -370 | -480 | -370 | -1,369 | -2,469 | -1,040 |
| Regular + PEUC + EB + State EB + PUA | -1,494 | -359 | -863 | 199 | -481 | -49 | -670 | 20 | -670 | -3,138 | -5,289 | -1,504 |
| Nonfarm Payrolls | 610 | | | | 245 | | | | | 711 | 610 | 245 |
| Household Employment | 2,243 | | | | -74 | | | | | 275 | 2,243 | -74 |
| Household Employment that Mimics Payrolls | 2,358 | | | | -51 | | | | | -248 | 2,358 | -51 |
| Unemployment | -1,519 | | | | -326 | | | | | -970 | -1,519 | -326 |
| Unemployment Rate | 6.9 | | | | 6.7 | | | | | 7.9 | 6.9 | 6.7 |

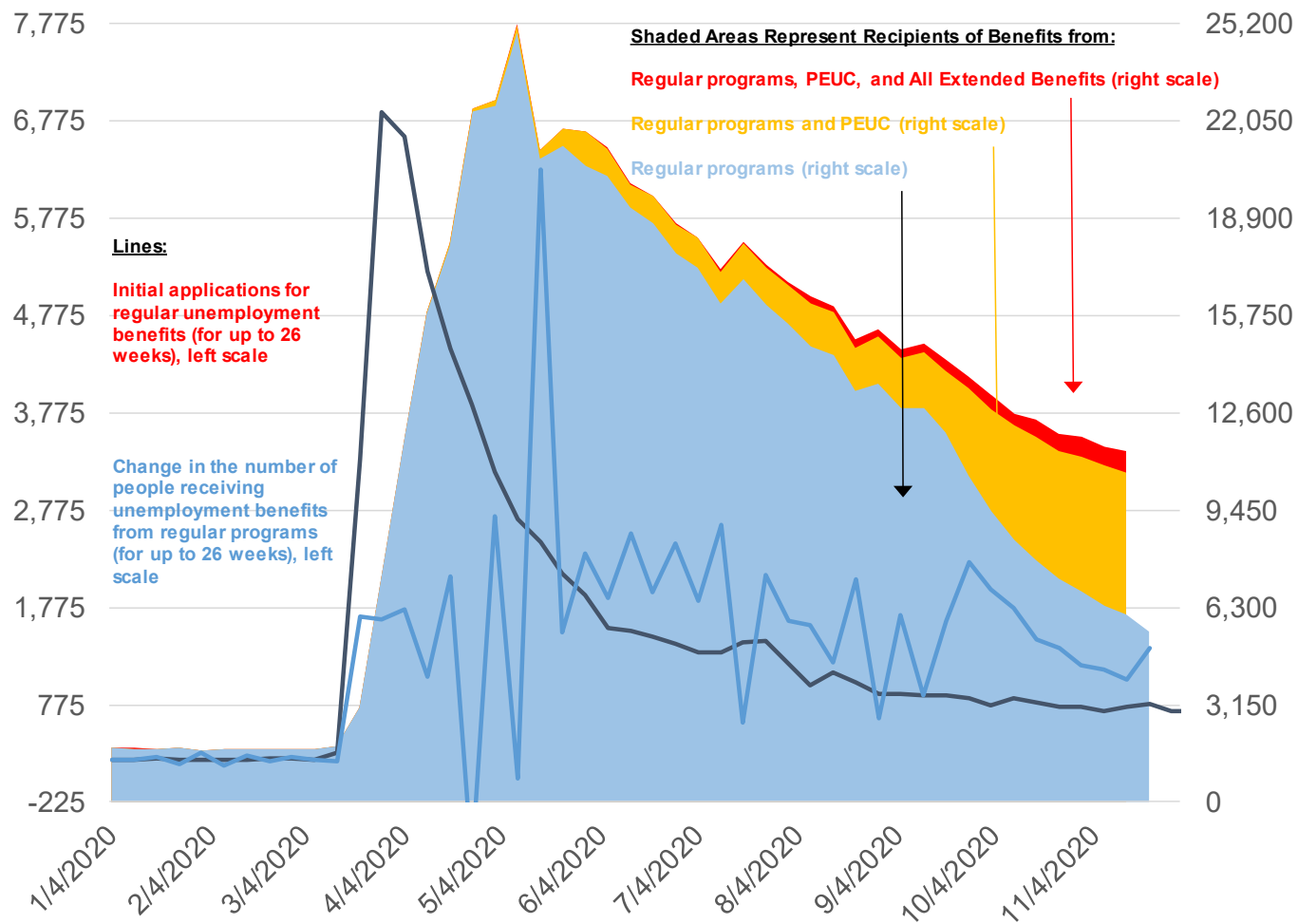
Notes: Regular - 26 weeks of benefits from regular state programs; PEUC = Pandemic Emergency Unemployment Compensation; EB - Extended Benefits; State EB - additional state unemployment benefits
Line enclosed in borders is most closely aligned with changes in employment and unemployment. Figures in bold, underlined and italics are forecasts for missing weeks.

Sources: Haver Analytics; U.S. Department of Labor. Updated through November 14, 2020 (extended benefits), November 21, 2020 (claimants), and November 28, 2020 (claims).

Timely, Comprehensive, Accurate, Detailed ...

Jobless claims and change in recipients ('000)

Recipients of all UI benefits ('000)

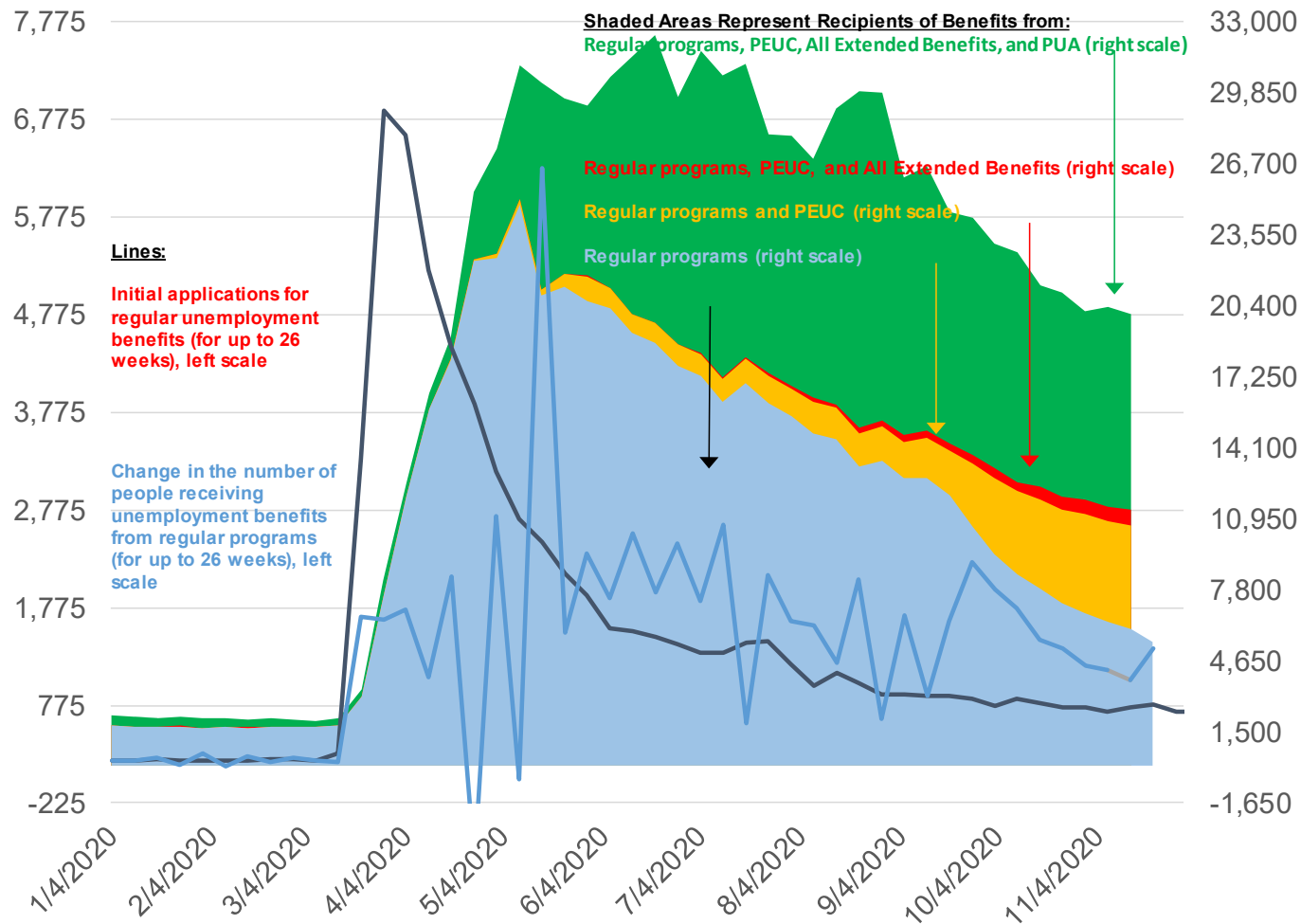


Sources: Haver Analytics; U.S. Department of Labor. Updated through November 14, 2020 (extended benefits), November 21, 2020 (claimants), and November 28, 2020 (claims).

... but Not PUA Flows ...

Jobless claims and claimants changes ('000)

Recipients of all UI benefits ('000)



Sources: Haver Analytics; U.S. Department of Labor. Updated through November 14, 2020 (extended benefits), November 21, 2020 (claimants), and November 28, 2020 (claims).

... Because Self-Employed Are Different

(Unincorporated) self-employment (thousands)



Sources: Haver Analytics; U.S. Department of Labor. Updated through October 2020.

Everyone Looks Similar

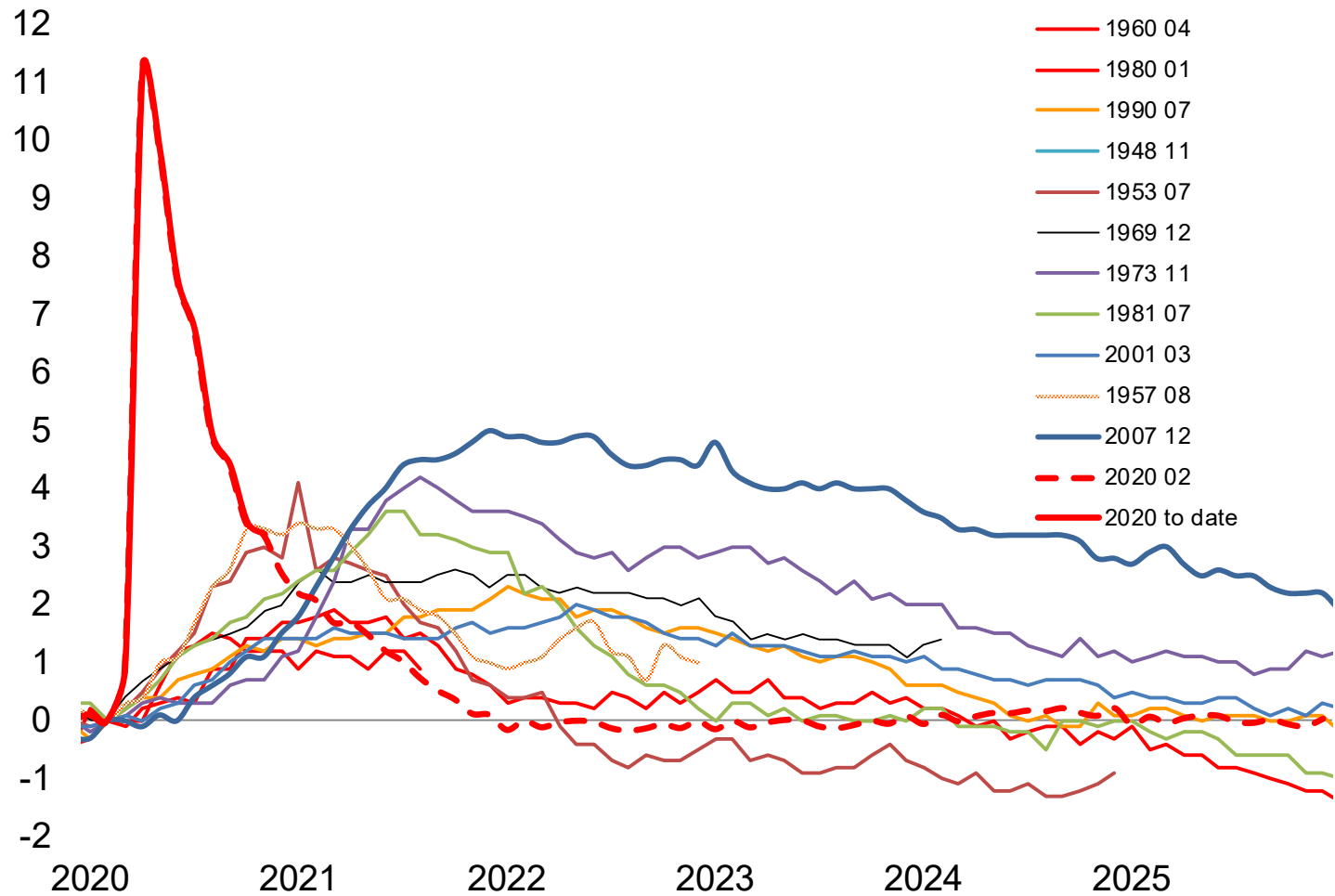
| Real GDP | Annualized% change from the previous quarter | | | | | Percent change over the four quarters of each year | | | | | | Steady State ¹ |
|--------------------|--|---------|-------|-------------|--------------|--|------|------|--------------|------------|------------|---------------------------|
| | 2019 Q4 | 2020 Q1 | Q2 | Q3 | Q4 | 2017 | 2018 | 2019 | 2020 | 2021 | | |
| Global | 2.0 | -10.1 | -27.1 | 31.8 | 3.8 | 3.7 | 2.7 | 2.5 | -2.7 | 4.1 | | |
| Global (PPP Basis) | 2.3 | -12.5 | -19.2 | 22.9 | 6.5 | 3.8 | 3.0 | 2.9 | -1.9 | 4.1 | | |
| Nafta | 2.0 | -5.2 | -33.1 | 35.1 | 2.9 | 2.7 | 2.4 | 2.1 | -3.1 | 3.1 | | |
| Canada | 0.6 | -8.2 | -38.7 | 46.4 | 3.0 | 3.2 | 1.8 | 1.5 | -4.0 | 2.8 | 2.0 | |
| Mexico | -2.5 | -4.9 | -52.4 | 58.0 | 4.0 | 1.8 | 1.3 | -0.7 | -7.1 | 1.9 | 2.5 | |
| United States | 2.4 | -5.0 | -31.4 | 33.1 | 2.8 | 2.7 | 2.5 | 2.3 | -2.8 | 3.2 | 1.8 | |
| Europe | 1.0 | -0.4 | -47.9 | 51.5 | -5.0 | 3.2 | 1.3 | 1.4 | -7.1 | 5.0 | 1.5 | |
| EU-28 | 0.4 | 0.4 | -50.3 | 54.5 | -5.7 | 3.1 | 1.5 | 1.2 | -7.7 | 5.4 | 1.5 | |
| France | -0.9 | -21.7 | -44.6 | 95.4 | -15.0 | 3.1 | 1.4 | 0.7 | -7.9 | 6.0 | 1.5 | |
| Germany | -0.1 | -7.4 | -33.8 | 38.5 | -4.0 | 3.6 | 0.3 | 0.4 | -5.0 | 4.8 | 1.5 | |
| Italy | -0.9 | -20.2 | -45.0 | 64.2 | -0.2 | 1.9 | 0.2 | 0.1 | -7.9 | 2.4 | 1.5 | |
| Spain | 1.7 | -19.4 | -54.3 | 85.5 | -8.0 | 3.1 | 2.3 | 1.7 | -11.0 | 7.7 | 1.5 | |
| United Kingdom | 0.6 | -9.7 | -58.7 | 78.0 | -8.0 | 1.6 | 1.2 | 1.0 | -11.6 | 9.0 | 1.5 | |
| Asia | 3.9 | -21.3 | -5.2 | 21.4 | 10.2 | 5.1 | 4.2 | 3.8 | -0.2 | 4.5 | | |
| Japan | -7.1 | -2.3 | -28.8 | 21.4 | 8.0 | 2.6 | -0.3 | -0.7 | -2.3 | 2.2 | 0.8 | |
| China | 6.4 | -40.0 | 46.8 | 10.8 | 11.9 | 6.7 | 6.4 | 5.8 | 2.2 | 5.0 | 7.5 | |
| India | 3.5 | 2.7 | -68.8 | 117.1 | 19.0 | 7.2 | 5.7 | 4.1 | -4.6 | 7.2 | 6.0 | |
| Korea | 5.4 | -5.0 | -12.0 | 8.0 | 4.0 | 2.9 | 3.2 | 2.4 | -1.6 | 4.1 | 4.0 | |
| Taiwan | 6.6 | -4.1 | -2.8 | 16.6 | 3.0 | 3.9 | 1.3 | 3.9 | 2.9 | 3.4 | | |
| Indonesia | 4.8 | -2.7 | -25.0 | 13.0 | 5.0 | 5.1 | 5.2 | 4.9 | -3.6 | 5.0 | | |
| Singapore | 0.6 | -3.1 | -43.2 | 42.3 | 3.5 | 2.8 | 0.8 | 0.8 | -5.1 | 5.4 | | |
| Hong Kong | 2.2 | -20.2 | -72.2 | 175.0 | 7.0 | 2.0 | 4.9 | 1.3 | -10.1 | 2.3 | | |
| Australia | 2.2 | -1.0 | -25.2 | 10.1 | 7.9 | 2.4 | 2.2 | 2.3 | -3.2 | 3.4 | | |
| Other | 1.0 | -2.8 | -21.8 | 23.4 | 4.8 | 3.0 | 2.1 | 2.0 | -0.4 | 3.7 | | |
| Brazil | 2.2 | -9.5 | -33.5 | 40.0 | 3.0 | 2.4 | 0.8 | 1.6 | -3.5 | 1.1 | 3.3 | |

¹ Maximum growth rate when the economy is close to full employment.

Source: Economic Research, Corporate Investment Bank, JPMorgan Chase & Co.

“We’ll be Home for Christmas” ... 2021

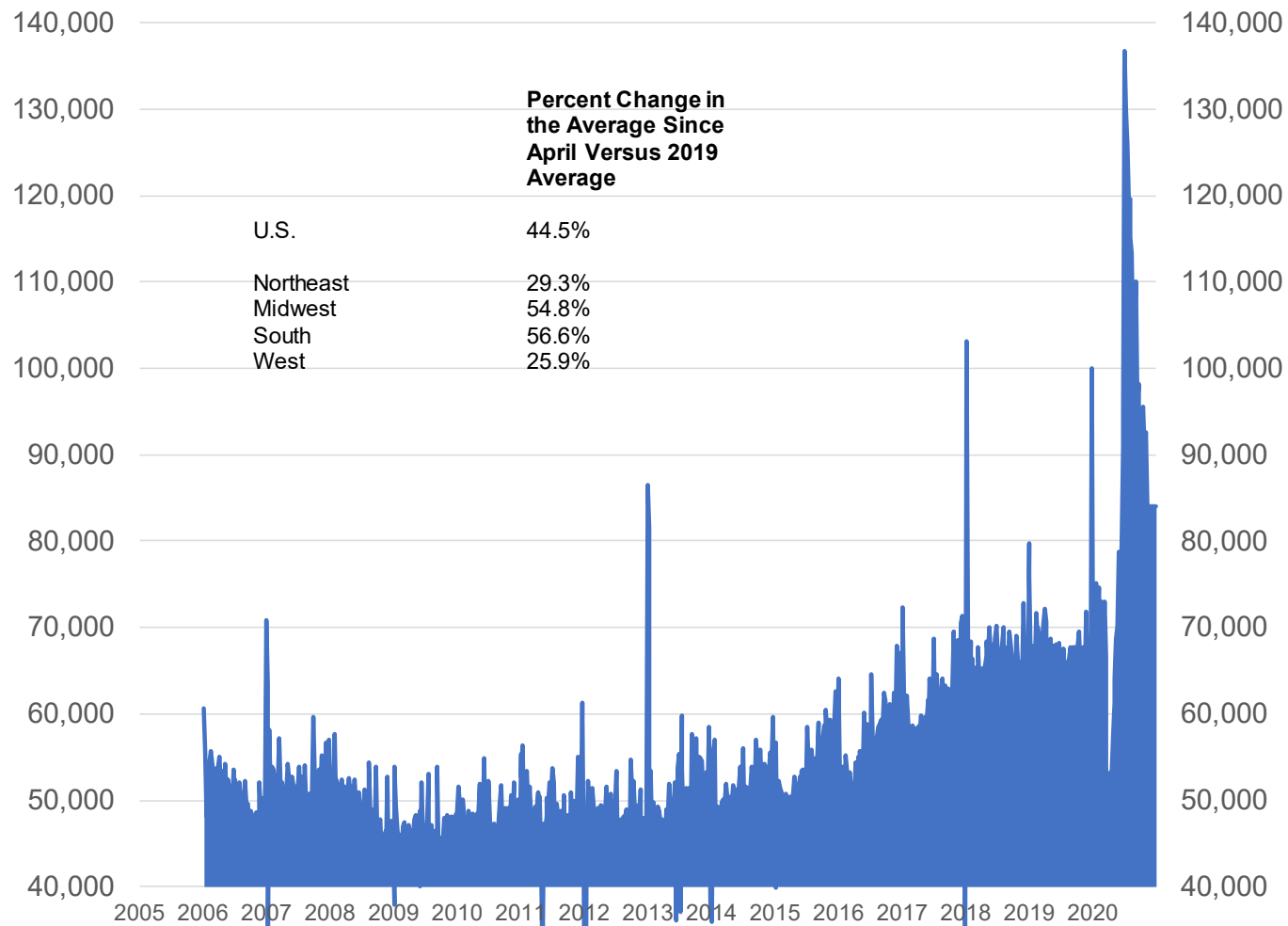
Unemployment rate (percent of the labor force)



Sources: Haver Analytics; U.S. Department of Labor. Updated through November 2020.

Turmoil Often Brings Opportunity

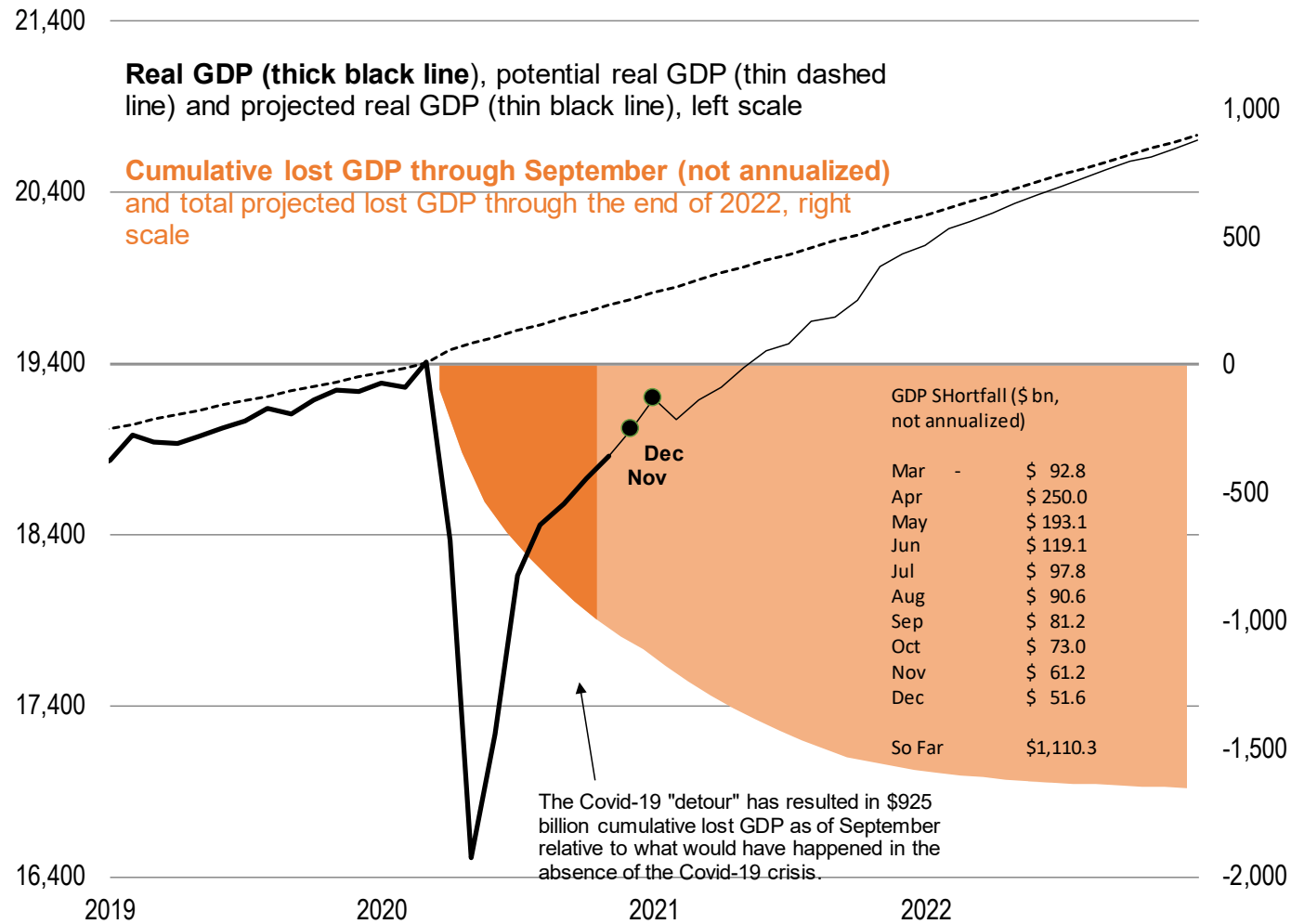
Applications to start new businesses (number)



¹ Includes: all applications for an Employer Identification Number, except filings, applications with no state-county geocodes, applications from certain agricultural, public entities, and applications in certain industries
Sources: Haver Analytics; Census Bureau. Updated through November 7 2020.

Reality Check

Real GDP (billions of chained 2012 dollars)



Sources: Haver Analytics; HIS Markit. Updated through October 2020 (GDP).

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M&A Market Updates

MCM Capital Markets Group /
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December 2020

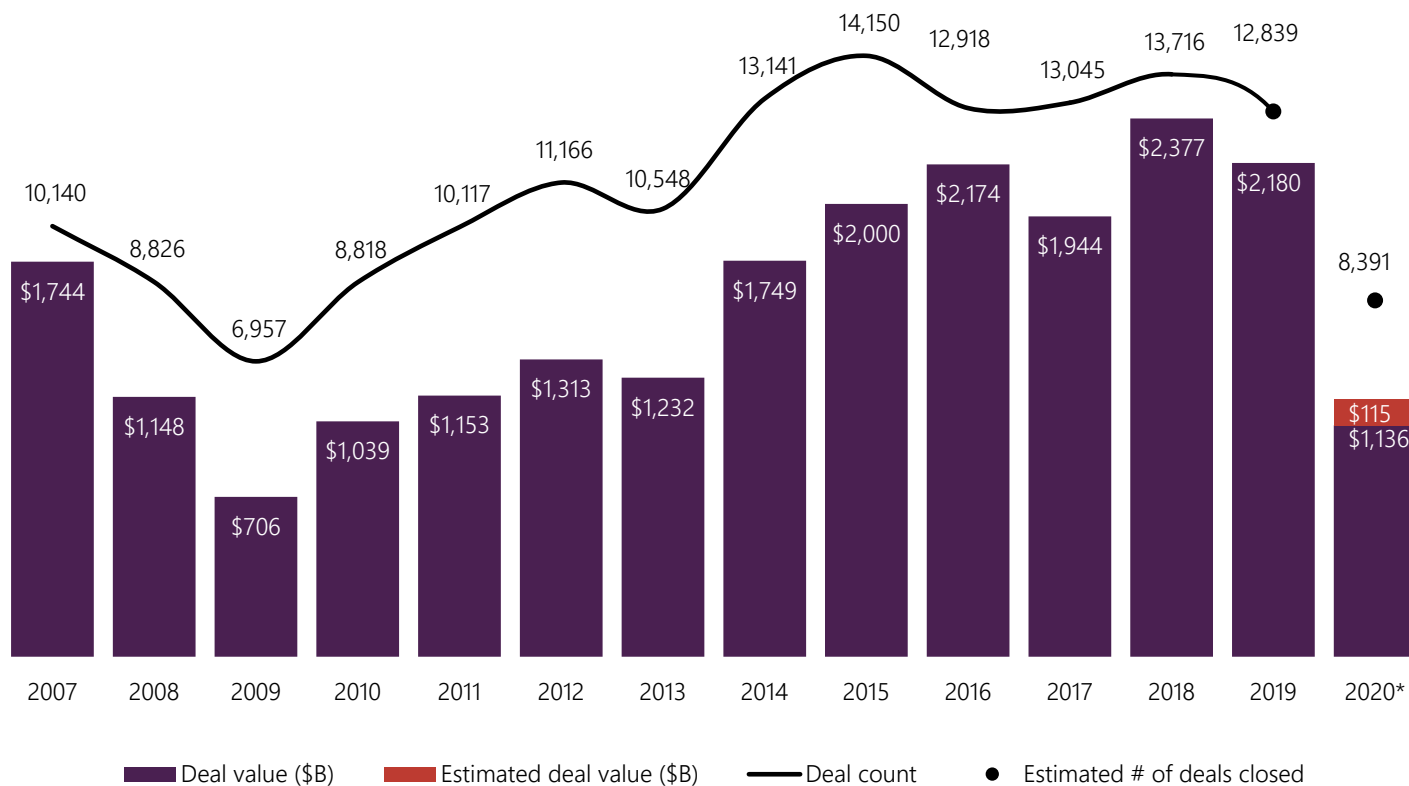
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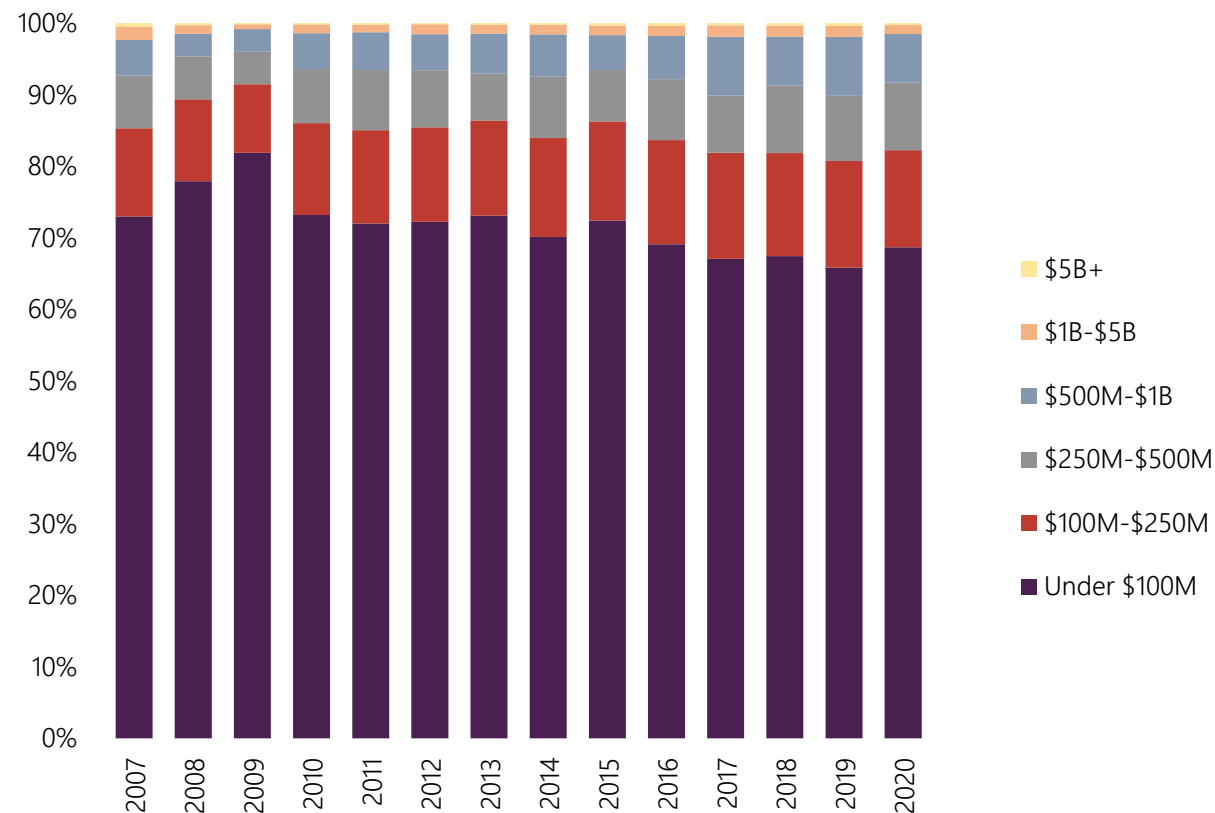
North American M&A Activity



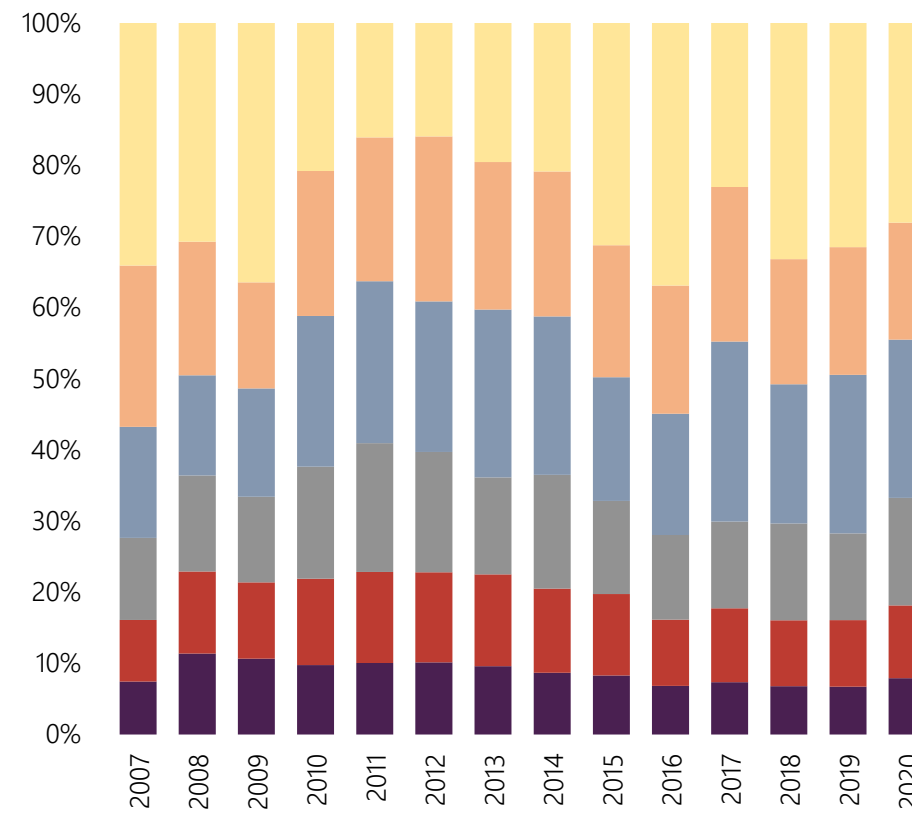
- Q'3 transaction volume increased over Q'2
- Compared with CY'19, overall deal valuations are down slightly, but deal volume remains off
- Healthcare accounts for 13.1% of total deal count in CY'20 – the highest percentage on record
- Trading multiples for technology deals remains strong, while aggregate transaction multiples lag the prior year
- Deal making in Q'3 was largely made up of transactions considered to be “smaller” in the North American M&A universe
- Deals under \$100m accounted for 68.7% of all M&A in CY'20 through Q'3

Source: Pitchbook NA Q3 2020 M&A

North American M&A Activity



of M&A deals by size



Transaction Value (\$'s) of M&A deals by size

Source: Pitchbook NA Q3 2020 M&A

Valuation Overview \$10m - \$250m EV

Trending Multiple Data

| All Transactions | 1Q19 | 2Q19 | 3Q19 | 4Q19 | 1Q20 | 2Q20 | 3Q20 |
|--------------------|------|------|------|------|------|------|------|
| # of Deals | 91 | 78 | 62 | 71 | 88 | 34 | 50 |
| TEV/EBITDA | 6.8x | 7.2x | 7.3x | 7.1x | 7.3x | 7.4x | 6.7x |
| Total Debt/EBITDA | 4.0x | 4.0x | 3.9x | 3.9x | 3.9x | 3.3x | 3.7x |
| Senior Debt/EBITDA | 3.5x | 3.2x | 2.9x | 3.2x | 3.5x | 2.8x | 2.7x |

Total Enterprise Value (TEV) / EBITDA

| TEV | CY'03-05 | CY'16 | CY'17 | CY'18 | CY'19 | YTD CY'20 | Total | N = |
|---------|----------|-------|-------|-------|-------|--------------|-------|-------|
| 10-25 | 5.6x | 5.8x | 6.3x | 5.9x | 6.1x | 6.1x | 5.7x | 1,432 |
| 25-50 | 6.2x | 6.4x | 6.6x | 6.9x | 6.9x | 6.8x | 6.4x | 1,081 |
| 50-100 | 6.8x | 7.2x | 8.2x | 8.8x | 7.5x | 8.1x | 7.3x | 736 |
| 100-150 | 7.4x | 8.8x | 9.1x | 8.7x | 9.4x | 9.1x | 8.2x | 385 |
| Total | 6.2x | 6.7x | 7.2x | 7.2x | 7.1x | 7.2x | 6.5x | |
| N = | 2,361 | 243 | 267 | 289 | 302 | 172 | | 3,634 |

Total Enterprise Value (TEV) / EBITDA by Industry

| Industry | CY'03-05 | CY'16 | CY'17 | CY'18 | CY'19 | YTD CY'20 | Total | N = |
|----------------------|----------|-------|-------|-------|-------|--------------|-------|-------|
| Manufacturing | 6.0x | 6.1x | 6.8x | 6.9x | 6.6x | 6.9x | 6.2x | 1,523 |
| Business services | 6.1x | 7.3x | 7.3x | 7.1x | 7.1x | 6.9x | 6.5x | 753 |
| Health care services | 6.9x | 7.6x | 8.1x | 7.8x | 8.4x | 7.8x | 7.3x | 332 |
| Retail | 6.3x | 7.0x | 7.3x | 7.5x | 9.3x | 7.4x | 6.8x | 111 |
| Distribution | 6.2x | 7.2x | 7.6x | 7.0x | 7.1x | 7.9x | 6.6x | 371 |
| Media & Telecom | 7.1x | 6.5x | 7.7x | 7.8x | 7.0x | 8.8x | 7.2x | 59 |
| Technology | 7.1x | 7.4x | 9.9x | 9.6x | 10.0x | 8.5x | 8.0x | 121 |
| Other | 5.8x | 6.9x | 6.5x | 7.0x | 6.6x | 6.3x | 6.1x | 364 |
| N= | | | | | | | | 3,634 |

- EV \$10 - \$250m – deal volume = 80% of the same period prior year
- Average valuations eased slightly in Q3
- The step back in valuation occurred in the \$25m+ EV sized companies, while \$10m - \$25m saw a slight increase in valuation

Please note that N for 2003-15 encompasses thirteen years of activity.

Seller considerations

- Seller's market
- Understand COVID impact on operations, suppliers and vendors
- What operational efficiencies can be retained
- Expect heavy diligence
- Prepare adjusted historical and normalized projected revenue, EBITDA, capital expenditures
- Higher adjusted cashflow = higher multiple
- Growth through acquisition as a selling strategy
- Expect an earnout
- Financial and strategic buyers are everywhere, if you don't like the conversation you're having with a prospective buyer and you are ready to sell, talk to another

Buyer considerations

- What is your positioning with regard to COVID and the impact on the seller's business
- Understand COVID impact on operations
- Understand COVID impact on suppliers and vendors
- Prepare an Executive Summary about your company and why you are the best fit for the seller
- Use an earnout to protect against downward trending or COVID revenues
- PPP loans
- Seller's market
- Be prepared - If the target doesn't feel comfortable with where the conversation is going, there is another buyer waiting in line
- Plan for heavy due diligence

EBITDA Addback Specifics

- EBITDA adjustments can have a positive or negative effect.
- There will always be the usual addbacks:
 - Compensation
 - Rent
 - Other Perks
- COVID adds a whole different level of adjustments.
- For some businesses, the adjustments could actually be detrimental for the business if the business has prospered during this pandemic.
- Understanding the COVID impact on current operations is key but also consider whether COVID has changed your business model.
- How COVID has impacted your customer base and your suppliers has a direct impact on your business. This should be accounted for in a valuation, EBITDA and budgeting and forecasts.

EBITDA Addback Specifics

- What are some of the specific adjustments we are seeing during this pandemic?
 - Step back and take a look at the business pre-COVID. Does your business look different?
 - Expenditures for PPE equipment and precautionary measures.
 - Lost revenues / profits due to low staffing and not being able to meet customers demands.
 - Overhead and administrative expenses not incurred due to the pandemic.
 - Impact of PPP loans and potential forgiveness on net working capital.
 - Impact of customer payments for receivables and cash inflows.
 - Impact of supplier shortages. Have you had to build up inventory? Is inventory higher because of the necessity to accumulate?
 - Has the business benefited from COVID? If so, you should normalize this performance.

MCM CMG Investment Banking Group



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Partner

Angela Marshall is a Partner in the Louisville office of MCM Capital Markets Group.

Angela focuses her practice in mergers and acquisitions within the firm’s consulting group. She provides full-service investment banking services to middle-market clients in the Kentucky, Indiana, and Ohio regions. Angela has more than 25 years of experience in assisting owners in transitioning their businesses, including buying and selling businesses, turnaround, and financial management. Prior to joining MCM, Angela worked as a director for Corporate Finance Associates, a worldwide middle-market investment banking firm. Angela has owned her own commercial construction and real estate company. Throughout her career, she’s worked on M&A transactions in broadcasting, healthcare, banking, manufacturing, distribution, technology, business services, and construction.

EDUCATION

M.B.A., University of Kentucky
B.S., Western Kentucky University



MCM CPAs & Advisors



Drew Chambers,
CPA-ABV, CFF, CFE
Partner

Drew Chambers is a Partner in the Louisville office of MCM CPAs & Advisors.

Drew has more than 20 years of experience in various assurance and consulting capacities while working with numerous businesses in industries including manufacturing, retail, construction, professional services, and publicly-traded companies. His previous experience as a member of the Audit and Assurance Services Group includes oversight of audit, attestation, and consulting engagements for a range of clients in a variety of industries. Drew now focuses his expertise within the firm's consulting group. His current practice is devoted primarily to business valuation for purposes of gift and estate tax areas, mergers and acquisitions, marital dissolutions, and succession planning. Drew also works closely with the legal profession and has served as an expert witness on litigation support projects involving business disputes, lost profits, and economic damages. He also assists businesses in the areas of fraud risk assessments, fraud and forensic examinations, and due diligence analysis for mergers and acquisitions.

EDUCATION

University of Louisville – Bachelor of Science in Accounting
Certified Public Accountant (CPA)
Accredited in Business Valuation (ABV)
Certified in Financial Forensics (CFF)
Certified Fraud Examiner (CFE)





Family Business Advisory Services

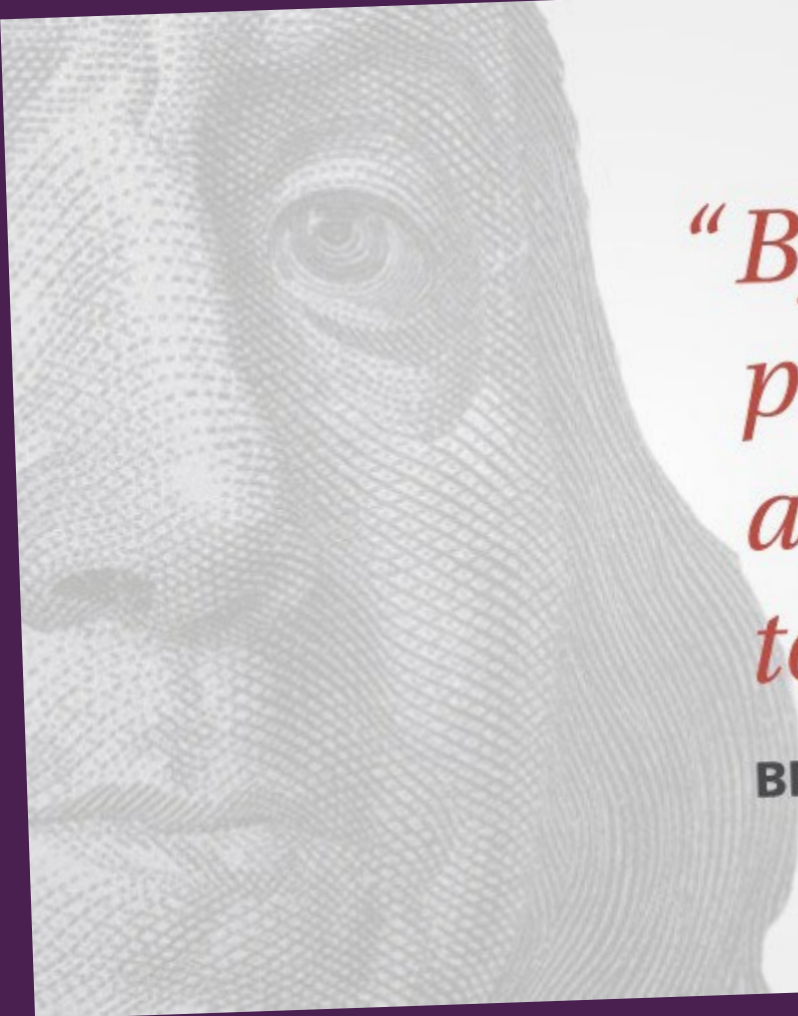
ANNUAL UPDATE
December 2020

Kathleen Hoye

Family Business Overview

- + 90% of all businesses in North America
- + 78% of all new job creation
- + 35% of fortune 500 companies (not just mom n pops)
- + 30% make it to 2G; number is dropping (20%)
- + 90% of families control or contribute to more than one firm (family enterprise model)





*“By failing to
prepare, you
are preparing
to fail.”*

BENJAMIN FRANKLIN

2019 Update: Family Firms

- + 1 in 10 of current FB leaders are Female (18% WW) ☹️
- + 2 in 10 have a robust succession plan
- + 4 in 10 have a retirement plan
- + 4 in 10 worried about digital disruption
- + 6 in 10 plan to pass to next generation of family
- + 6 in 10 of the next CEOs will be MILLENNIALS
- + 6 in 10 have an emergency/contingency plan
- + 8 in 10 expect steady growth in next two years
- + 8 in 10 involve directors in strategic growth planning

Source: University of Louisville, PWC,



The Technology Divide

- + 61% of Next Gens say technology/digital are the most important drivers of change for their FB
- + 25% say their business is worse than competitors at using technology effectively
- + 40% say they match their competition
- + 90% say having a business strategy “fit for the digital age” requires significant or incremental change in their FB

Source: Family Firm Institute



“Crossing the COVID 19 Crisis”

- + Theme of 2019 STEP Global Family Business Survey
- + STEP: Successful Transgenerational Entrepreneurship Practices
- + 1,834 participants from 33 countries



Best Practices: Crisis Survival

| Business | Family |
|---|-------------------------------------|
| Crisis Competencies and Agile Crisis Structure | Values work, Alignment and Cohesion |
| Countercyclical Investing and Courageous Change Processes | Family Governance |
| Communication, Exchange, and Networking | Engagement and Competencies |



3 or more = Higher Entrepreneurial Performance

| Governance Practice | Global % | North America % |
|-----------------------------|----------|-----------------|
| Women on the board | 31 | 34 |
| Formal succession process | 16 | 18 |
| Formal bylaws | 16 | 21 |
| Formal BOD | 11 | 8 |
| Board of Advisors | 7 | 5 |
| Different share classes | 6 | 8 |
| Mandatory retirement age | 6 | 1 |
| External directors on board | 5 | 2 |
| Majority external directors | 3 | 3 |



Recommendations

1. **Codify your values and purpose into your strategy.** If this is where your family business has a competitive edge, take it to the next step.
2. **Ensure the next generation is deeply involved** - they have a lot to offer families grappling with digitalization.
3. **Determine the skill sets needed for a more digital future.** Raising the 'Digital IQ' of the business is closely entwined with raising digital capabilities of existing workforce and determining future skill sets. With 80% of US CEOs expecting AI to significantly change the way they do business in the next five years, the race for talent will only intensify. US family business leaders are aware of the challenges, keeping and rewarding employees are seen as top priorities.
4. **Professionalize the board** by bringing in independent directors with external expertise in future growth areas for your business.



5. Plan your inevitable exit from the business!



*“By failing to
prepare, you
are preparing
to fail.”*

BENJAMIN FRANKLIN

Summary

Informal governance is going to make success in today's economy more difficult for family businesses. They're still in a strong position. They've built up trust among loyal employees and their ownership group. Yet in the absence of a deliberate plan for success in a more digital economy or without the benefit of outside expertise, staying loyal to the employees and continuing profitable growth is going to be tough.

—Jonathan Flack

US Family Business Leader



Thank You!

Kathleen Hoye

Consulting Principal

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Kathleen is a Principal in the Consulting Services Team at MCM CPAs & Advisors. She has had extensive experience helping and advising firms with their growth, development and passing enterprises to the next generation. Her areas of focus include business strategy; family and business governance; family and business policy development; succession planning; leadership development; next generation career coaching; family education and communication; and exit planning that allows owners to exit their businesses on their terms and conditions.

Before working at MCM, she was the Director of the Family Business Center at the University of Louisville and Director of the Small Business Development Center for North Central Kentucky. She also created the Vogt Invention and Innovation Fund for the Vogt family in Louisville, which provides seed stage support and capital for inventors and product developers as well as co-launching the award-winning radio series This I Believe on NPR.

Kathleen is a frequent presenter at family business and trade conferences, educational programs and meetings covering topics such as family governance, change management, succession planning, exit planning, leadership development and family communication.

Education & Certifications

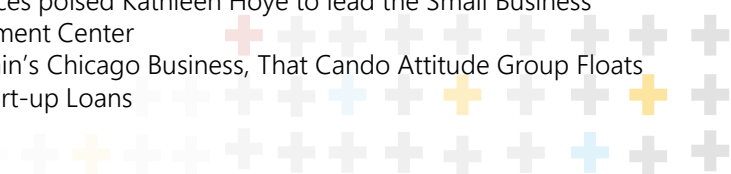
- Five Behaviors Team Cohesion
- University of Illinois – Master's Degree, Urban Planning and Policy
- Valparaiso University – B.A., Communications and World History
- Certified Exit Planner (CEXP)
- Advanced Certificate in Family Business Advising (ACFBA)
- Certified in Family Wealth Advising (CFWA)

Professional and Community Associations

- Family Firm Institute (Fellow)
- Business Enterprise Institute (BEI)
- Psychodynamics of Family Business (PDFB)
- UofL Family Business Center
- Greater Louisville, Inc.
- Goering Center for Family and Private Business
- Old National Center for Closely Held Business

Lecturer and Author

- Regular Presenter, Psychodynamics of Family Business Conference, Chicago
- 2016, Family Firm Institute Annual Conference Presenter
- Family Business Magazine
- 2014, Entrepreneur Magazine, 7 Lessons in Harmony for Family Startups
- 2010, Business First, Family Businesses are the Cathedrals of our Economy
- 2008, Business First of Louisville, Bound by Synchronicity: Varied experiences poised Kathleen Hoye to lead the Small Business Development Center
- 1994, Crain's Chicago Business, That Cando Attitude Group Floats Small Start-up Loans





Accounting & Auditing Update

December 8, 2020

Presenters



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Session Topics

+ COVID – Certain A&A Considerations

+ A&A Update

+ Lease Standard Update



COVID-19: Accounting & Financial Reporting

Possible Impact Areas

- + CARES Act Government Assistance
- + Sub. Events/Disclosure Considerations
- + Going Concern
- + Debt Modifications
- + Leases
- + Income Tax Considerations
- + Estimates
- + Asset Impairments
- + Revenue Recognition
- + Exit and Disposal Costs
- + Loss Contingencies
- + Benefits
- + Recognition of Interest Income
- + Hedging
- + Income Statement Classification
- + Risks and Uncertainties



PPP Loan Summary (as of 08/08/2020; SBA)

| | |
|-----------------------|-------------------|
| Approved Loans | 5,212,128 |
| Approved Dollars | \$525,012,201,124 |
| Average Size of Loan | \$101,000 |
| Participating Lenders | 5,460 |



Accounting & Audit Considerations

+ PPP Loans

- + Most entities will be past their covered periods by 12/31/2020
- + Accounting method
- + Confirmation
- + Liability classification (current vs. non-current)
- + Deferred income tax issues
- + Test forgiveness calculation
- + Analysis more extensive for loans > \$2 million



Accounting & Audit Considerations

(Continued)

- + Asset Impairments – Long-lived Assets
 - + According to New Constructs, LLC:
 - + Impairment charges totaled ~\$261B 1H2020
 - + 129% amount recorded for all of 2019
 - + Not just a year-end issue
 - + Impairment test required when events indicate that long-lived assets may not be recoverable (triggering event)
 - + Once impairment loss is recorded, it cannot be reversed
 - + Based on general impairment indicators, many entities likely to conclude that triggering event has occurred in 2020



Accounting & Audit Considerations

(Continued)

- + Asset Impairments – Long-lived Assets
 - + Possible relief: Option to perform goodwill triggering event evaluation only on annual reporting date
 - + Limited to private companies and NFPs that only prepare GAAP-compliant financial statements on an annual basis
 - + FASB voted 11/18 to add project.
 - + Drafting exposure draft (expected Q4 2020)
 - + Best case – final end of Q1 2021
- + Asset Impairments - Inventory
- + Asset Impairments – Investments
- + Collectability and recognition of bad debts



Engagement Considerations

- + Remote working conditions can make many aspects more challenging
- + Sufficient evidence is required to support audit opinion
- + Use of video conferencing
- + Substantive analytics - pandemic effects
 - + May not be appropriate this year
- + Impact on internal control
 - + Possible breakdowns this year - change to work from home impact
 - + Increased fraud risks



Engagement Considerations

- + Increased risk of noncompliance with laws and regulations
- + Inventory observation
- + Use of electronic signatures
- + Availability of SOC 1 reports
 - + Possible scope limitation



Accounting Standards

| Number | Description | Private | Public |
|---------|---|--------------------|-------------------|
| 2017-08 | Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities | 12/15/19 | Already Effective |
| 2017-11 | Earnings Per Share (Topic 260) Distinguishing Liabilities from Equity (Topic 480) Derivatives and Hedging (Topic 815): I. Accounting for Certain Financial Instruments with Down Round Features | 12/15/19 Part 1 | Already Effective |
| 2018-07 | Compensation—Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting | 12/15/19 | Already Effective |
| 2019-08 | Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer | 12/15/19 | Already Effective |



Accounting Standards

| Number | Description | Private | Public |
|---------|---|--------------------|-------------------|
| 2018-13 | Fair Value Measurement (Topic 820) Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement | 12/15/19 | 12/15/19 |
| 2019-03 | Not-for-Profit Entities (Topic 958): Updating the Definition of Collections | 12/15/19 Part 1 | Already Effective |
| 2019-04 | Codification Improvements to Topic 326, Financial Instruments—Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments | 12/15/19 | Already Effective |
| 2020-03 | Codification Improvements to Financial Instruments | 12/15/19 (some) | Already Effective |
| 2020-04 | Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting | Issuance | Issuance |



ASU 2018-07

- + ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting
- + Issued June 2018
- + Brings the accounting together for both employee and nonemployee share-based payment transactions into FASB ASC 718, *Compensation-Stock Compensation*
- + Deletes FASB ASC 505-50, *Equity-Equity-Based Payments to Nonemployees*
- + **Substantive changes for entities that grant share-based payment awards to nonemployees**



ASU 2018-07

- + Number of amendments, aimed at simplifying accounting
 - + Nonpublic entity - one-time election to switch from measuring liability-classified nonemployee share-based payment awards at fair value to intrinsic value
 - + Regardless of the election, liability-classified awards would be subject to remeasurement until exercise
- + Effective for public companies for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year
- + For all other companies, effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2019
- + Early adoption is permitted, but no earlier than a company's adoption date of FASB ASC 606



ASU 2019-08

- + ASU 2019-08, *Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*
- + Issued November 2019
- + What does it do?
 - + Clarifies accounting related to share-based payments issued in conjunction with selling goods or services under FASB ASC 606, Revenue from Contracts with Customers
- + Why was it issued?
 - + Diversity in practice in applying the guidance related to noncash awards in FASB ASC 606 or the guidance in other parts of the Codification (FASB ASC 718)



ASU 2019-08

- + Share-based payment awards granted to customers should be accounted for following the guidance in FASB ASC 718, *Compensation- Stock Compensation*
- + Awards should be measured at the grant date
- + Classification and measurement of awards also accounted for in accordance with FASB ASC 718
 - + Unless award is subsequently modified and recipient is no longer a customer
- + Income statement classification not modified; still a reduction of transaction price



ASU 2018-13

- + ASU 2018-13, *Fair Value Measurement (Topic 820) - Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*
- + Issued August 2018
- + Updates disclosure requirements required related to fair value measurements
 - + Some disclosures, removed, added, or modified
 - + Some changes are not applicable to nonpublic entities



ASU 2018-13

+ Nonpublic entity impact

+ New Disclosures: NONE!

+ Eliminated Disclosures:

- + Valuation process for Level 3 fair value measurements
- + Policy for timing of transfers between levels of the fair value hierarchy
- + Changes in unrealized gains/losses included in earnings for recurring Level 3 fair value measurements held at the end of the reporting period



ASU 2018-13

+ Modified Disclosures

| Topic | Legacy U.S. GAAP | Amended U.S. GAAP |
|---|----------------------------------|--|
| Liquidity events for investments in entities that calculate NAV | Estimate and disclose the timing | Only disclose if investee has communicated the timing to the company or announced publicly (also applicable for PBEs) |
| Level 3 rollforward | Required to be disclosed | No longer required, instead disclose: <ul style="list-style-type: none"> • Transfers in/out • Purchases/ issuances |

+ Eliminate “at a minimum” from the phrase “an entity shall disclose at a minimum” to promote the appropriate exercise of discretion and clarify that materiality is an appropriate consideration when evaluating disclosure requirements



ASUs To Consider for Early Adoption

- + ASU 2018-14, *Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*
- + Issued August 2018
- + Applicable to all employers that sponsor defined benefit pension or other postretirement plans
- + Remove, modify, and add disclosures to make them clearer and more beneficial to users



ASUs To Consider for Early Adoption

- + ASU 2018-15, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement (CCA) That Is a Service Contract*
- + Issued August 2018
- + Provides guidance on the accounting for implementation costs incurred to implement a hosting arrangement that is a service contract
- + Does not change the accounting for the service element of a hosting arrangement that is a service contract



ASUs To Consider for Early Adoption

- + ASU 2018-17, *Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities*
- + If certain conditions are met, a private company may choose not to apply the VIE consolidation guidance to legal entities under common control
- + Additional disclosures about involvement with and exposure to each common control party
- + Issued October 31, 2018



ASUs To Consider for Early Adoption

- + ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*
- + Issued December 2019
- + What does it do?
 - + Simplifies areas of FASB ASC 740 which are costly and complex to implement while maintaining usefulness of information
- + Why was it issued?
 - + Feedback received from stakeholders as part of the simplification initiative



ASUs To Consider for Early Adoption

- + ASU 2020-07, *Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets*
- + Issued September 2020
- + What does it do?
 - + Requires separate presentation of contributions of nonfinancial assets as well as additional disclosures related to the same
 - + Does not change recognition and measurement for gifts-in-kind
- + Why was it issued?
 - + To address stakeholder concerns about the lack of transparency related to how certain gifts-in-kind are valued and used



Lease Accounting Update




Thank You

For Your Time!



MCM COVID-19 Resource Center

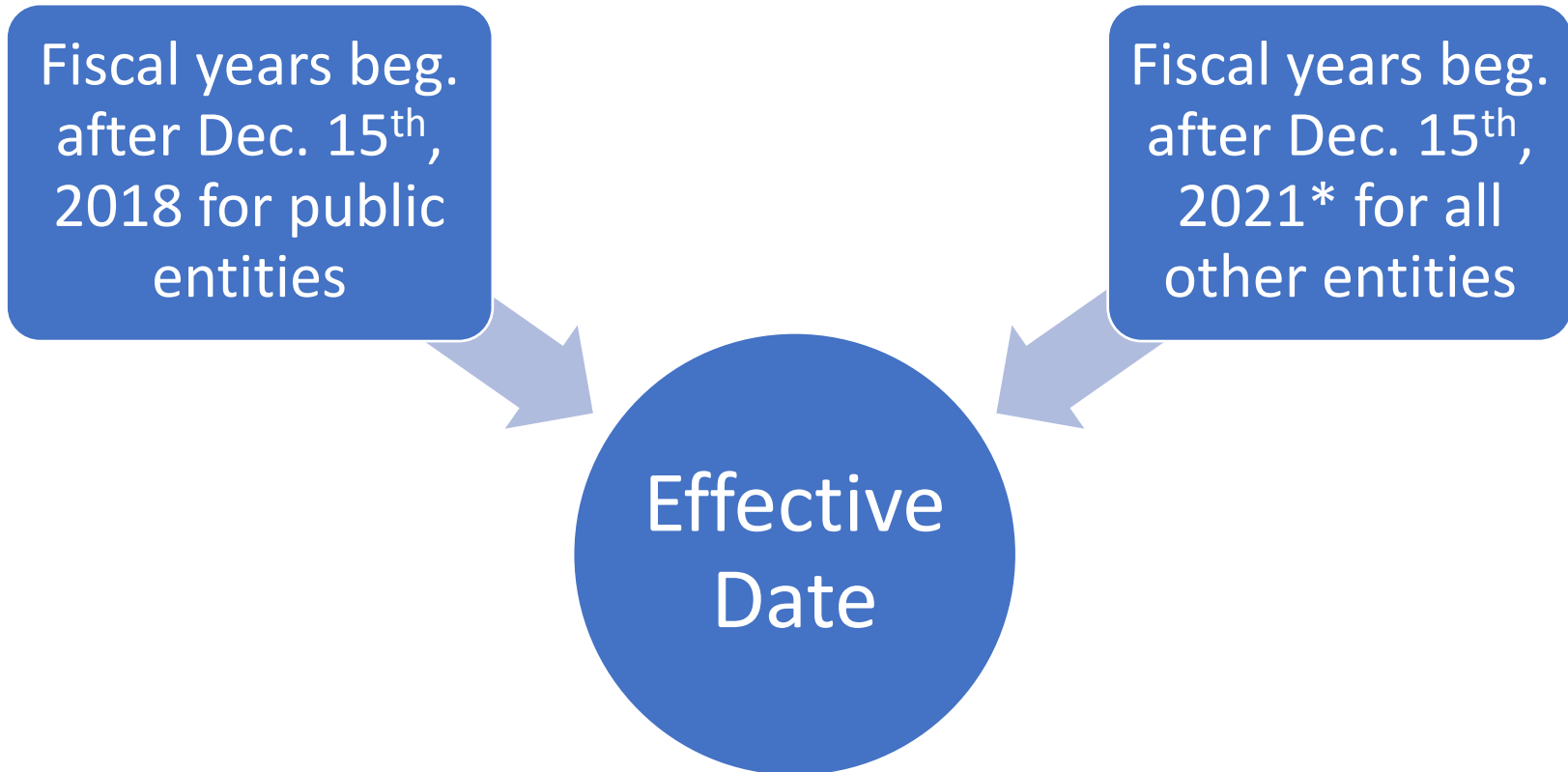
www.mcmcpa.com/covid-19



Leases 842 Project – New Developments and Implications (ASU 2016-02)

Scott Maloy, CPA

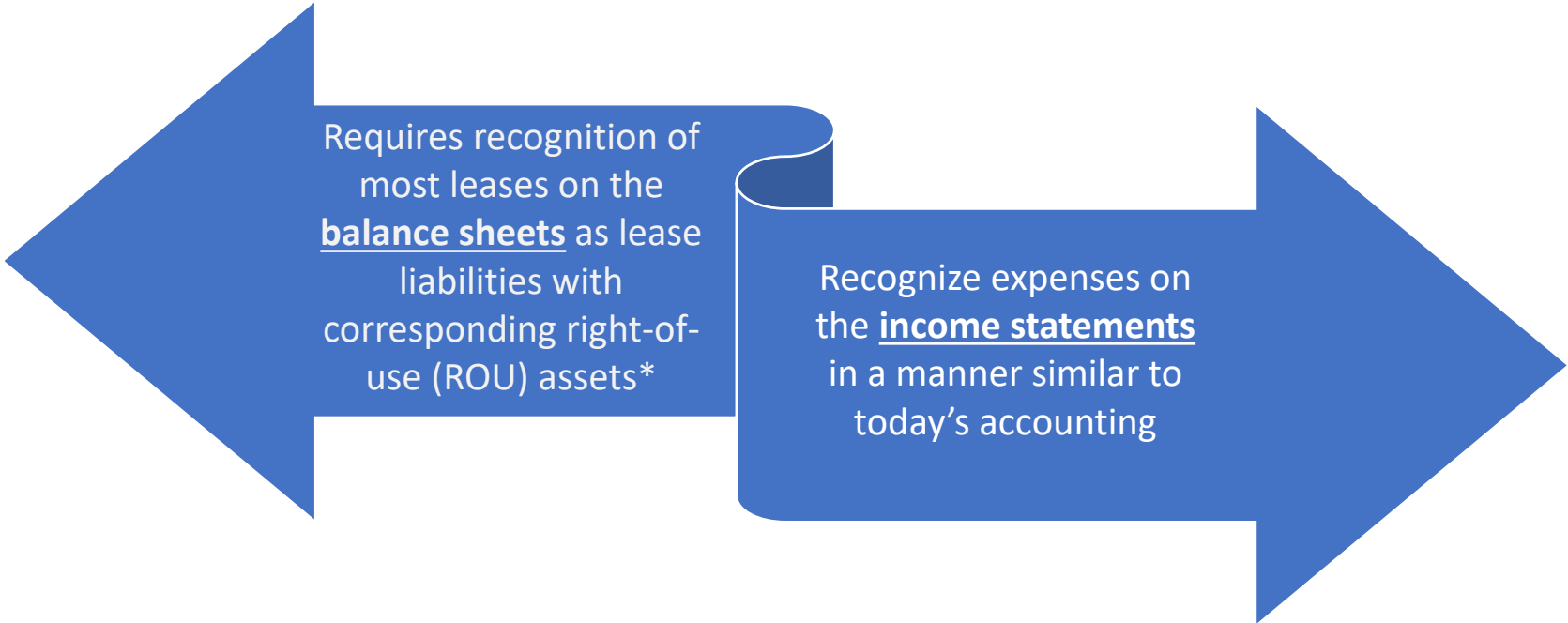
Timing



Note: Most debt agreements will be renewed prior to effective date.

** Considers recent delay afforded by ASU 2020-05*

Key Changes - Lessee



Requires recognition of most leases on the **balance sheets** as lease liabilities with corresponding right-of-use (ROU) assets*

Recognize expenses on the **income statements** in a manner similar to today's accounting

*Requires impairment testing for new ROU assets



Comparison of Lessee Accounting Models

Finance Lease

Balance Sheet

Right of Use (ROU) Asset*
Lease Liability

Income Statement

Interest Expense (on lease liability)
Amortization Expense (on ROU asset)

Cash Flow

Cash paid for principal payments (financing activities) & interest payments (operating activities)

*Periodically reduced by straight-line amortization

Operating Lease

Balance Sheet

Right of Use (ROU) Asset**
Lease Liability

Income Statement

Lease/Rent Expense (straight-line)

Cash Flow

Cash paid for lease payments

**Periodically reduced by the difference between straight-line lease expense & interest cost on lease liability, *i.e.*, “plug figure”

ASC 842 Effects Illustrated

| | <u>Current</u> | <u>ASC 842</u> | <u>Diff.</u> |
|------------------------|------------------|------------------|------------------|
| Current Assets | 2,500,000 | 2,500,000 | - |
| Noncurrent Assets | <u>5,000,000</u> | <u>6,275,000</u> | <u>1,275,000</u> |
| Total Assets | 7,500,000 | 8,775,000 | 1,275,000 |
| Current Liabilities | 1,500,000 | 1,845,000 | 345,000 |
| Noncurrent Liabilities | <u>5,000,000</u> | <u>5,930,000</u> | <u>930,000</u> |
| Total Liabilities | 6,500,000 | 7,775,000 | 1,275,000 |
| Equity | 1,000,000 | 1,000,000 | - |

Current ratio

1.67

1.36

Debt to equity

6.50

7.78



Example Language in Debt Agreements

MODIFICATION OF CREDIT AGREEMENT. The Credit Agreement is hereby amended as follows:

- 2.1 Section 5.4 of the Credit Agreement captioned "Financial Statement Calculations" is hereby amended and restated to read as follows:
- 5.4 **Financial Statement Calculations.** The financial covenant(s) set forth in Section 5.3 entitled "Financial Covenants", except as may be otherwise expressly provided with respect to any particular financial covenant, shall be calculated on the basis of the Borrower's financial statements prepared on a consolidated basis with its Subsidiaries in accordance with GAAP, provided that, if after the date hereof there occurs any change in GAAP or in the application thereof on the operation of any provision hereof and the Bank notifies the Borrower that the Bank requests an amendment to any provision hereof for such purpose, regardless of whether any such notice is given before or after such change in GAAP or in the application thereof, then such provision shall be interpreted on the basis of GAAP as in effect and applied immediately before such change shall have become effective until such provision is amended in accordance herewith. Notwithstanding the foregoing, for purposes of determining compliance with any financial covenant contained herein, the effects of FASB Accounting Standards Update 2016-02 (Topic 842) shall be disregarded.



Trends:

+ Fallout:

+ Cost  than anticipated

+ Complexity  than anticipated

+ Software – when is it needed?



Trends (cont.):

+ Transition:

- + Impact – JE likely

- + Method

 - + Almost all did NOT adjust PPs. (ASU 2018-11)

- + Practical Expedients

 - + Package of Three

 - + Lease and non-lease components:

 - + **Example from Wayfair, Inc.:** "The Company has lease arrangements with lease and non-lease components. For the Company's warehouse and fulfillment center lease arrangements, the Company accounts for lease and non-lease components separately. For all other lease arrangements, the Company accounts for lease and non-lease components as a single lease component."



Trends (cont.):

+ Discount rate

+ 840 vs 842 definition change

+ Few using implicit rate and challenges to determine IBR

- + **Wayfair, Inc.:** "As most of the Company's leases do not provide an implicit rate, the Company uses its estimated incremental borrowing rate based on the information available at commencement date in determining the present value of future payments. The determination of the Company's incremental borrowing rate requires judgment. The incremental borrowing rate for each lease is primarily based on publicly-available information for companies within the same industry and with similar credit profiles. The rate is then adjusted for the impact of collateralization, the lease term and other specific terms included in the Company's lease arrangements. The incremental borrowing rate was determined at lease commencement, or as of January 1, 2019 for operating leases existing upon adoption of ASC 842."

+ Private Company election option: risk-free rate

Trends (cont.):

+ Disclosures

- + Enable users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases including significant judgments in applying the requirements.

- + Same for all entities

+ New:

- + Information about leases that have not yet commenced but that create significant rights and obligations for the lessee, including the nature of any involvement with the construction or design of the underlying asset.
- + Information about significant assumptions and judgments made in applying the requirements of FASB ASC 842, which may include the following:
 - + 1. The determination of whether a contract contains a lease
 - + 2. The allocation of the consideration in a contract between lease and nonlease components
 - + 3. The determination of the discount rate for the lease

Trends (cont.):

+ Disclosures

+ New:

- + Short-term lease cost, excluding expenses relating to leases with a lease term of one month or less
- + Variable lease cost
- + Weighted-average remaining lease term
- + Weighted-average discount rate
- + A lessee shall disclose a maturity analysis of its finance lease liabilities and its operating lease liabilities separately, showing the undiscounted cash flows on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years. A lessee shall disclose a reconciliation of the undiscounted cash flows to the finance lease liabilities and operating lease liabilities recognized in the statement of financial position.

Concessions

- + Hardships caused by COVID-19
- + Rent concessions
 - + Deferral of payments
 - + Reduction of payments
 - + Rent forgiveness
- + Under 840 or 842 this would typically trigger modification accounting of the lease.
- + Lease modification analysis can be:
 - + Costly
 - + Burdensome
 - + Complex



Concessions (cont.)

- + FASB has allowed relief via an accounting policy election
 - + Only available for COVID-19 lease concessions that result in the total consideration required by the contract being substantially the same as, or less than, the total consideration originally required by the contract.
 - + Applied enterprise-wide or for leases with similar characteristics or circumstances (i.e. class of assets or similar types of concessions in similar lease arrangements).
 - + Must be agreed upon by the parties involved in the lease
 - + Required disclosures



Concessions (cont.)

| Deferral of Lease Payment | Expense Compared to Original Pattern | Change to Lease Liability? |
|--|---|----------------------------|
| 1. Note payable | Same | No |
| 2. Negative variable lease payment | Deferred (less up front and more on back end) | No |
| 3. Remeasurement consistent with resolving a contingency | Same | Yes |



Concessions (cont.)

| Payment reductions | Expense Compared to Original Pattern | Change to Lease Liability? |
|--|--|----------------------------|
| 1. Note payable | N/A | N/A |
| 2. Negative variable lease payment | Less in the period of rent reduction | No |
| 3. Remeasurement consistent with resolving a contingency | Less but evenly spread over remaining lease life | Yes |

- Assistance:
- Lease analysis consulting
 - Lease calculations and maintenance



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PEOPLE
MATTER



LEADERS
INSPIRE



EXCELLENCE
RULES

IRS Circular 230 Disclosure.

+ As a result of perceived abuses, the Treasury has recently promulgated Regulations for practice before the IRS. These Circular 230 regulations require all accountants to provide extensive disclosure when providing certain written tax communications to clients. In order to comply with our obligations under these Regulations, we would like to inform you that any advice given in this presentation, including any attachments, cannot be used to avoid penalties which the IRS might impose, because we have not included all of the information required by Circular 230, nor have we performed services that rise to this level of assurance.



Paycheck Protection Program (PPP) Loans - Accounting

December 8, 2020

Presenter



Todd M. Hamilton

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Assurance Partner

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MCM CPAs & Advisors

+ **What We Do:**

+ **MCM is a large regional CPA and advisory firm employing more than 350 individuals, including more than 160 CPAs. We serve both privately and publicly held businesses, small businesses, non-profit organizations, governmental entities, and individuals.**

+ **Mission: We exist to help both our clients and team succeed.**

Core Values



People Matter – We genuinely care about our people, personally and professionally, and ensure relevance in their work.



Leaders Inspire – We inspire each other to sustain our vision and advance our mission as a firm.



Excellence Rules – We are committed to superb client service, high quality expertise and significant client relationships.



PPP Loans - In General

- + Economic need; loan necessity questionnaires - all PPP loans of \$2M or more
- + Largely unknown how the U.S. Small Business Administration (SBA) will interpret; use of hindsight
- + Uncollateralized/unsecured; interest at 1%; 24-60 month maturity dates
- + Spend on eligible payroll costs plus 25% attributable to specific (leases; utilities; interest) non-payroll expenses during the covered period (8/24 weeks)
- + Up to 100% forgiveness based on the loan recipient meeting the employee retention criteria and other related conditions/ requirements, including economic need
- + Submit the forgiveness application to the lending bank; the bank has up to 60 days
- + Upon bank approval, the SBA has up to 90 days to review (potentially) and approve/deny

Business Entities

- + For commercial for-profit business entities, there is **no specific guidance** under accounting principles generally accepted in the United States of America (U.S. GAAP) on how to account for this type of loan or the related loan forgiveness
- + For commercial for-profit business entities, there is **no** specific Financial Accounting Standards Board (FASB) standard
- + There is some flexibility
- + Which accounting treatment is most appropriate for the company's unique circumstances and/or to the users of the financial statements



Business Entities (Continued)

- + **FASB Accounting Standards Codification (ASC) Topic 470, *Debt***
 - Record the cash inflow from the PPP loan as a financial liability (debt)
 - Accrue interest in accordance with the interest method under FASB ASC 835-30
 - Would not impute additional interest at a market rate (even though the stated interest rate may be below market)
 - Continue to record the proceeds from the loan as a liability until either [1] **the loan is partially or fully forgiven and the debtor has been legally released** or [2] the debtor pays-off the loan
 - Reduce the liability by the amount forgiven and record a gain on extinguishment once the loan is partially or fully forgiven **and legal release is received**
 - Potential bank debt covenant considerations



Business Entities (Continued)

- + **A grant by analogy to International Accounting Standard (IAS) 20, *Accounting for Government Grants & Disclosure of Government Assistance***
 - If the entity expects to meet the eligibility criteria and concludes the PPP loan represents, in substance, a grant that is expected to be forgiven, the recipient may analogize to IAS 20
 - Under this model, government assistance is not recognized until there is **reasonable assurance (reasonable assurance is not defined; is similar to the "probable" threshold in U.S. GAAP; generally interpreted as "likely" / 75% or greater likelihood of occurrence)** that [1] any conditions attached to the assistance will be met (**loan eligibility criteria**) and [2] the assistance will be received (**loan forgiveness criteria**)
 - Record the cash inflow from the PPP loan as a deferred income liability
 - Once there is reasonable assurance the conditions will be met, the earnings impact of government grants is recorded **on a systematic basis over the periods in which the entity recognizes as expenses the related costs for which the grants are intended to compensate**
 - Subsequent to initial recognition, the entity would reduce the liability, with the offset through earnings (presented as either **[1] a credit in the income statement, either separately or under a general heading such as "other income,"** or [2] a reduction of the related expenses) (**expense off-set is however contrary to U.S. GAAP**), as it recognizes the related costs to which the loan relates

Business Entities (Continued)

+ A grant by analogy to FASB ASC 958-605, *Not-for-Profit Entities: Revenue Recognition*

- FASB ASC 958-605 addresses the accounting for contributions by not-for-profit entities
- Although the scope of FASB ASC 958-605 excludes contributions made by governmental entities to business (for-profit) entities, FASB has acknowledged that entities scoped out of this guidance are not precluded from applying it by analogy when appropriate
- The timing of recognition for a contribution received depends on whether the contribution is **conditional** or not
- If conditional, the contribution is not recognized until the conditions are **substantially met (substantially met is not defined; is somewhat vague)** or explicitly waived
- The entity would initially record the cash inflow from the PPP loan as a refundable advance
- The entity would then reduce the refundable advance and recognize the contribution once the conditions of release (the related barriers) have been **substantially met** or explicitly waived
- The barriers (economic need; eligible expenditures; meeting the full-time equivalent requirements; completion of the 8 or 24 week covered period; the submission of the forgiveness application; approval from the lending bank and/or the SBA; etc.) may be different by company/entity

Business Entities (Continued)

+ A grant by analogy to FASB ASC 450-30, *Contingencies: Gain Contingencies*

- FASB ASC 450-30 outlines a model for gain contingency recognition
- The earnings impact of a gain contingency is recognized **when all the contingencies related to receipt of the assistance have been met** and the gain is realized or realizable
- The entity would initially record the cash inflow from the PPP loan as a liability
- The proceeds from the loan would remain recorded as a liability until the grant proceeds are realized or realizable, at which time the earnings impact would be recognized
- FASB ASC 450-30 generally provides less specificity on measurement and recognition requirements as compared to the other models/options
- Likely similar accounting to FASB ASC Topic 470

Not-for-profit Entities

- + If a NFP chooses not to follow FASB ASC 470 and expects to meet the eligibility criteria and concludes the PPP loan represents, in substance, a grant that is expected to be forgiven, the NFP should account for the PPP loan in accordance with **FASB ASC 958-605** as a conditional contribution



Governmental Entities

- + Governmental Accounting Standards Board (GASB) Technical Bulletin No. 2020-1, *Accounting & Financial Reporting Issues Related to the Coronavirus Aid, Relief, & Economic Security (CARES) Act of 2020 & Coronavirus Diseases*
- + The provisions/requirements of GASB Technical Bulletin No. 2020-1 were effective upon issuance of the Technical Bulletin
- + Account for the PPP loan as a liability in accordance with GASB Statement 70, *Accounting & Financial Reporting for Non-exchange Financial Guarantees* (PPP loans are guaranteed through a non-exchange financial guarantee provided by the SBA), until the entity is **legally released from the debt**
- + The governmental entity should report an inflow of resources in the period in which the entity is legally released from the debt

All Entities

- + All entities with material PPP loans should adequately disclose their accounting policy for such loans and the related impact to the financial statements, including the statement of cash flows presentation
- + The U.S. GAAP/book and tax (when applicable) considerations should not be independently considered



Recap

- + FASB ASC 470 (debt); FASB ASC 450-30 (contingencies); GASB Technical Bulletin No. 2020-1 (governmental entities) - **likely forgiveness by the SBA**
- + IAS 20 (grant) - **reasonable assurance may not be clear for some companies/entities; reasonable assurance is not defined (similar to the "probable" threshold in U.S. GAAP)**
- + FASB ASC 958-605 (NFP contributions) - **conditions of release (the related barriers) have been substantially met; substantially met is not defined (vague); may be different by company/entity**
- + Comprehensive accounting policy note disclosure
- + The U.S. GAAP/book and tax (when applicable) considerations should not be independently considered



Paycheck Protection Program (PPP) Loans - Tax Issues

December 8, 2020

Presenter



Rick Woods

CPA

Tax Partner

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Loan Forgiveness Tax Issues

- + CARES Act - loan forgiveness income is not taxable income
- + IRS Notice 2020-32 - no deduction will be allowed for expenses paid with PPP loan proceeds (not what Congress intended)
- + Congress could act to restore the deduction through legislation, but, to-date, this has not yet occurred despite broad bi-partisan support



Loan Forgiveness Tax Issues (Cont.)

- + Timing dilemma - expenses paid in 2020, but many taxpayers have not yet applied for forgiveness and don't anticipate having their application approved by their bank and the SBA until 2021
- + In this situation, can you still deduct expenses in 2020 (and presumably recognize income under the tax benefit rule in 2021)?
- + The IRS has taken the position that if the taxpayer "reasonably expects to receive forgiveness," the expenses are not deductible in 2020 (Revenue Ruling 2020-27)
- + If reasonable uncertainty surrounding forgiveness still exists as of the filing date, should you take the deduction for the expenses on the 2020 return (and presumably disclose)?



Loan Forgiveness Tax Issues (Cont.)

- + What if the SBA ultimately doesn't forgive the loan?; Revenue Procedure 2020-51 provides the option to either:
 - + Deduct in 2020 on the originally filed or amended return, or
 - + Deduct in 2021
- + Consider how forgiveness will be accounted for U.S. GAAP/book purposes (remember IRC Section 451(b)(1)(C) conformity rule)
- + Consider the interaction with the R&D tax credit
- + *This is a tax planning nightmare!! Congress needs to fix this!!!*



Thank You

For Your Time!



MCM COVID-19 Resource Center

www.mcmcpa.com/covid-19



Risk Advisory Update

Kourtney Nett, Partner – Risk Advisory Services
Leader

December 8, 2020

Agenda.

- + COVID-19 impact on internal controls
- + Considerations for SOC report user entities
- + New SOC report opportunities



COVID-19 impact on internal controls

COVID-19 has changed how companies operate.

COVID-19 has resulted in significant changes to the operations, processes and workforce of companies, including:

- + Implementing a work-from-home policy
- + Restricting access to facilities
- + Reassigning responsibilities between employees and locations
- + Reducing the size of the workforce
- + Increasing the load on internet infrastructure such as VPN systems and firewalls
- + Delaying the implementation of additional processing capacity
- + Delaying the implementation of system changes



Impact on the risk assessment.

Updating your risk assessment is critical to assessing the effectiveness of existing controls and identifying the need for new controls in response to changing threats or vulnerabilities.

A few questions to ask:

- + What has changed in our operation?
 - + People, processes and technology
- + Which of our controls will continue to operate as previously designed regardless of changes to our operations?
- + Which controls are not operating as designed?



Impact on internal controls.

The following types of changes to a company's operations, processes and workforce should be considered:

- + Review the frequency and precision of controls
- + Segregation of duty implications
- + Documentation formats
- + Retention of evidence
- + Documentation of control and process changes
 - + Including communication to all impacted personnel
- + Revisit cybersecurity controls



Increased emphasis on understanding IT.

Auditing standards require the auditors to obtain an understanding of how a company uses IT and the impact of IT on the financial statements. Expect additional scrutiny on the following:

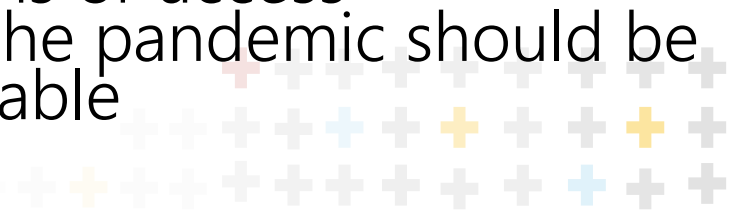
- + Implementation of new or modifications to existing technology to enable a remote work environment
- + Changes to Administrator or Super User accounts
- + Focus on access controls – changes and ongoing monitoring



Post-pandemic considerations.

After the COVID-19 pandemic has passed, consider the following:

- + Review lessons learned and decide whether internal controls can be enhanced based on experience gained during the pandemic
 - + Presents opportunity to challenge balance of manual and automated controls
- + Re-evaluate risk assessments
- + If controls or control frequencies that might have been reduced should be returned to normal
- + Any exceptional authorizations or access permissions granted during the pandemic should be revised or removed as applicable



Considerations for SOC report user entities

Considerations for SOC report user entities.

As a user of SOC reports, it is important to have frequent communication with your critical vendors to discuss whether COVID-19 has significantly impacted their operations or SOC report.

A few items to keep in mind:

- + Review the SOC report for disclosures on any changes to the system, operations or controls as a result of COVID-19
 - + Assess whether these changes impact you or your reliance
- + Review the SOC report for exceptions and expect some organizations may have increased exceptions due to the pandemic
 - + Put enhanced scrutiny around exceptions – could they be indicative of other control issues?
- + Review disclosures surrounding the impact of COVID-19 on subservice providers
- + Review the complementary user entity considerations and assess whether any additional considerations were added due to changes in the system description or controls



Newest additions to AICPA SOC suite

SOC for Cybersecurity.

- + Report is geared toward any organization, not just service organizations
- + Independent assessment of a company's cybersecurity risk management program
 - + Provides flexibility by not constraining management to a particular security management framework or control framework (i.e., NIST, ISO, SANS, etc.)
- + Deliverable is a general use report that is unrestricted for distribution
 - + Can be a Type I or Type II
- + Potential Report Users
 - + Business Partners, Investors, Board of Directors, Industry Regulators



SOC for Supply Chain.

- + Newest addition to the SOC suite
- + Provides assurance to user entities around the security and availability of products and information from suppliers within the supply chain
- + Details how the supplier's system produces, manufactures, or distributes products and how that system was designed and implemented based on a standard set of criteria (newly developed DC300)
- + Deliverable is a restricted use report (Type I or Type II) Potential Report Users
 - + Current and prospective business partners, investors, industry regulators
- + "Assess once, report many"





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PEOPLE
MATTER



LEADERS
INSPIRE



EXCELLENCE
RULES



Technology Update

Jim Kramer, Partner – Technology Solutions Team
Leader

December 8, 2020

Learning Objectives

- + Understand the impact of 2020 on Technology and networking.
- + Security Considerations for 2021
- + Resource Allocation and verification



Understand the impact of 2020 on
Technology and networking.



2020 and it's impact on Technology



- + Digital Adaption is increasing at a staggering rate
- + Forecasts for technology adoption are averaging over 1 year of forecasted adaption per month
- + Many sources are saying we will see 10+ years of new adoption between April and December.



Staying competitive requires a new strategy

+Biometrics

- + Enhance security
- + Health Screening

+Virtual Desktops

- + Eliminate physical presence requirements

+Communications

- + Conference Software exploding

+TeleHealth

- + Cleveland Clinic went from 2% to 75% virtual outpatient visits
- + Another health provider went from 100 telehealth visits a month to over 50000 per week in 2020



Which new technology will stay?

- +62% - Customer expectation of a technology presence
- +54% - Increase in remote work for staff
- +54% - Increase in migration to cloud services
- +53% - Increase in online purchases and services
- +53% - Increase in spend on data security
- +50% - Use of advanced technology in operations
- +49% - Use of Advanced technology in business decision making
- +48% - Development or enhancement of redundant supply chain



Strategic Posture toward IT

In 2017 - Scaling Down IT Expenses is a top 3 priorities – 48% companies

+In 2020 survey:

- +38% - Invest more \$ in technology to gain competitive advantage
- +30% - Modernize core technology capabilities
- +19% - Refocus business around digital technologies
- +10% - Look at ways to reduce IT spending
- +3% - Other top priority



How to adopt technology quickly

+ More tech resources

- + Good luck hiring the right resources
- + Outsourcing as a second option
- + Defined project work

+ New Technology is emerging everywhere

- + AI
- + Cloud Services (Software as a Service)
- + Virtual Desktops and Servers

+ Innovation

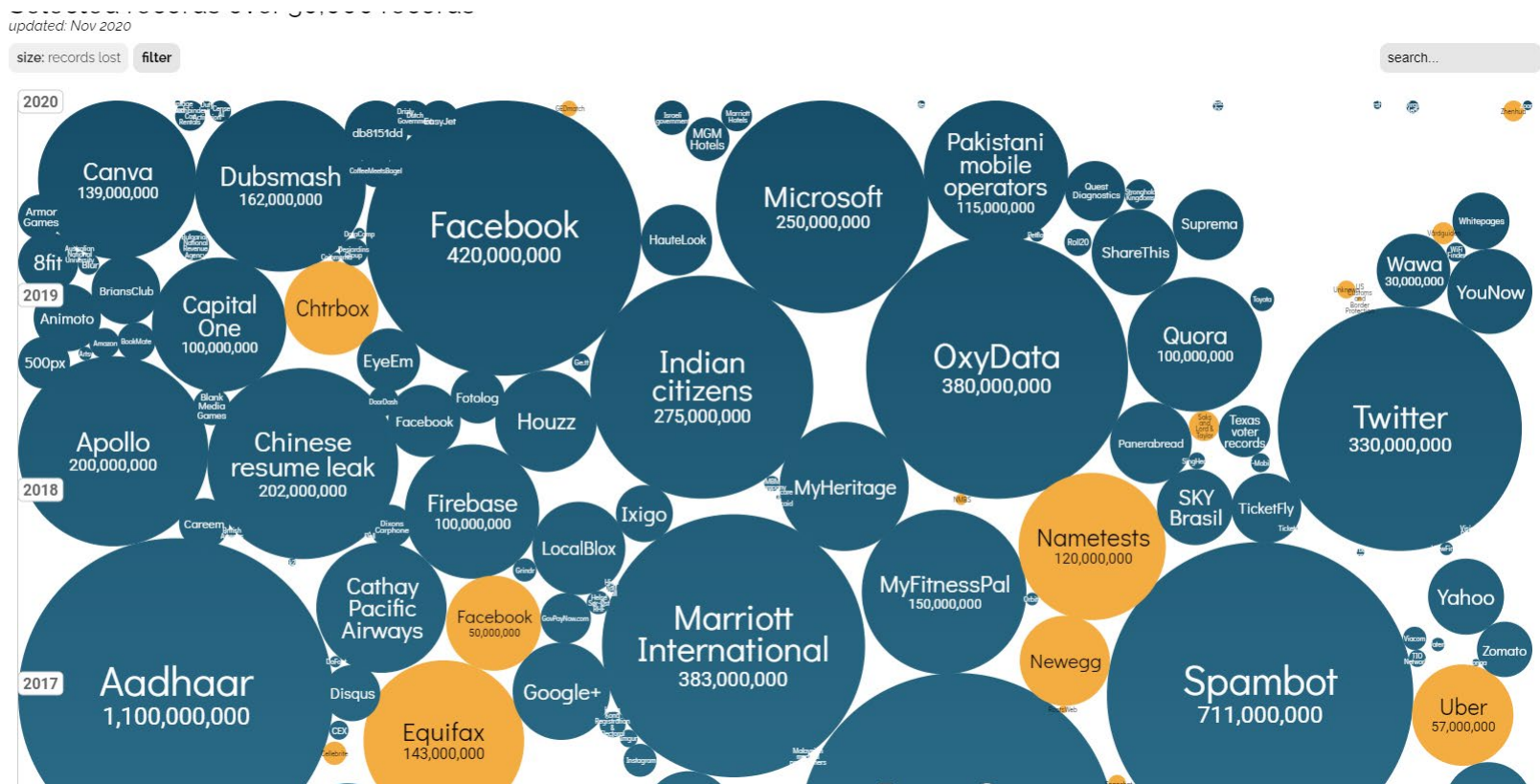
- + Speed of integrating new technology into an office
- + Determining which technology will assist and which is just “cool”



Security Considerations



What were some recent data breaches?



What does the hacker of today look like?



64% - State Sponsored or Organized Crime











30% - Insider Threats

6% - Individuals or Petty Thieves



Why do the hackers want your data?

Here are several examples of the price for your stolen data:

| | | | | |
|---|---|---|---|--|
|  Spotify Account \$2.75 |  Hulu Account \$2.75 |  Netflix Account \$1.00 - \$3.00 |  PayPal Credentials \$1.50 |  Social Security Number \$1.00 |
|  Driver's License \$20.00 |  Credit Card \$8.00 - \$22.00 |  Email Address & Password \$0.70 - \$2.30 |  Medical Record from Large Scale Attack \$1.50 - \$10.00 |  Complete Medical Record Up to \$1000.00 |



Changing Threat Landscape

- + Remote workforce
 - + No longer behind the corporate firewalls and defenses
- + BYOD
 - + Companies can not verify updates and protection of personal computers
 - + An often-overlooked threat to the organization
- + Social engineering
 - + Has become the number one attack vector
 - + Training is KEY with remote users.



What to do to protect the network

- + Maintain Security Policies
 - + Verify documentation
 - + Communicate policies
- + Verification
 - + Vulnerability Assessment
 - + Policy adherence and documentation
- + Prevention
 - + TRAINING
 - + Remote access
 - + Tools to protect data



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