

September 6, 2022

## MEETING OF THE AUDIT COMMITTEE OF THE BOARD OF DIRECTORS

FRIDAY, SEPTEMBER 9, 2022, 3:00 P.M.

**PLEASE NOTE:** Participation will be virtual pursuant to Palomar Health Board Resolution No. 01.10.22(03)-03 which applies to those members of the Palomar Health Development Board who are also members of the Palomar Health Board.

Please join the meeting from your computer, tablet or smartphone: <https://meet.goto.com/174294869>

OR Dial in using your phone: 877.309.2073; Access Code: 174294869#

	<u>Time</u>	<u>Page</u>	<u>Target</u>
I. CALL TO ORDER			3:00
II. PUBLIC COMMENTS <sup>2</sup>	15		3:15
<i>5 minutes allowed per speaker, with a cumulative total of 15 minutes per group For further details and policy see <a href="#">Request for Public Comment</a> notice on the website</i>			
III. INFORMATION ITEMS			
A. None	0		3:15
IV. OLD BUSINESS			
A. None	0		3:15
V. MINUTES			
*A. Monday, December 6, 2021 ( <i>Addendum A – Pp5-10</i> )	2	2	3:17
VI. NEW BUSINESS			
*A. Election of a Chairperson and a Vice-Chairperson of the Audit Committee	3	3	3:20
VII. PRESENTATIONS			
A. Audited Financial Statements – FYE June 30, 2022– ( <i>Addendum B – Pp11-21</i> ) Aldrich CPAs & Advisors LLP	20	4	3:40
VIII. COMMITTEE MEMBER COMMENTS/FUTURE AGENDA ITEMS	5	—	3:45
IX. FINAL ADJOURNMENT			3:45

Next Meeting: TBD

Palomar Health Development, Inc.  
Audit Committee of the Board of Directors

Linda C. Greer, RN, Director

Laurie Edwards-Tate, MS, Director

If you have a disability, please contact us 72 hours prior to scheduled meeting time  
by calling 760-740-6383 to arrange reasonable accommodations

**Minutes from the December 6, 2021,  
Palomar Health Development Audit Committee Meeting**

**TO:** Audit Committee of the Palomar Health Development Board

**MEETING DATE:** Friday, September 9, 2022

**FROM:** Tanya Howell, Corporate Secretary

**Background:** The minutes from the PHD Audit Committee meeting held on Monday, December 6, 2021, are respectfully presented for approval (*Addendum A*).

**Budget Impact:** N/A

**STAFF RECOMMENDATION:** Staff recommends approval of the minutes from the PHD Audit Committee meeting, held on Monday, December 6, 2021.

**Motion:** X

**Individual Action:**

**Information:**

**Required Time:**

## Election of Officers for CY2022

**TO:** Audit Committee of the Palomar Health Development Board

**MEETING DATE:** Friday, September 9, 2022

**FROM:** Michael J. Bogert, Chief Financial Officer

**Background:** The Bylaws of Palomar Health Development, Inc. (“Health Development”) {*ARTICLE IV, Section 4.12, as amended January 27, 2015*} authorize the Board of Directors (“the Board”) to create one or more Board committees. In November 2018, the Board formally created a two-person Audit Committee, comprised of “the two Palomar Health-appointed Directors of the Board not appointed Chairperson of the Board”.

Further, *ARTICLE IV, Section 4.13* requires that regular and special meetings and actions of Board Committees shall be governed by the provisions of this *Article IV* applicable to meetings and actions of the Board.

*ARTICLE IV, Section 4.07* requires that the Board elect officers at its Annual Organizational Meeting: “One member shall be elected as Chairperson, one as Vice-Chairperson and one as Secretary. The Board may also appoint the Treasurer at the Annual Organizational Meeting.” In order to adapt *Section 4.07* for pertinence to this two-person Board Committee, a Chairperson and a Vice-Chairperson should be elected.

**Budget Impact:** N/A

**STAFF RECOMMENDATION:** Staff recommends that a Chairperson and a Vice-Chairperson be elected for the Audit Committee of the Health Development Board.

**Motion:** X

**Individual Action:**

**Information:**

**Required Time:**

**Entrance Presentation of the External Auditing Firm  
Aldrich CPAs & Advisors LLP**

**TO:** Audit Committee of the Palomar Health Development Board

**MEETING DATE:** Friday, September 9, 2022

**FROM:** Hubert U. King, Chief Financial Officer

**Background:** The external auditing firm of Aldrich CPAs + Advisors LLP has been retained to perform an audit of the FYE June 30, 2022, financial reports of Palomar Health Development, Inc. Representatives from the firm will discuss the attached planned scope of the audit at the meeting (*Addendum B*).

**Budget Impact:** Budgeted

**STAFF RECOMMENDATION:**

**Motion:**

**Individual Action:**

**Information:** X

**Required Time:**

# ADDENDUM A

## Meeting Minutes

ATTENDANCE ROSTER		
MEMBERS	MEETING DATES	
	9/15/2021	12/6/2021
Linda Greer, RN		V
Jeff Griffith, EMT-P	E	V
<b>Staff Attendee</b>		
Tanya Howell, Secretary	V	V
<b>Former Members</b>		
John Clark	V	
<b>Guest Presenters<sup>1</sup></b>		

P = Present E = Excused V = Virtual

<sup>1</sup> See text of minutes for names of invited guests/presenters

**HEALTH DEVELOPMENT SPECIAL AUDIT COMMITTEE – MEETING MINUTES – MONDAY, DECEMBER 6, 2021**

**(I.A) AGENDA ITEM**

**• DISCUSSION**

**CONCLUSIONS/ACTIONS**

**FOLLOW-UP/  
RESP PARTY**

**I. CALL TO ORDER**

- **Notice of Meeting and Full Agenda Packet** were posted at PH’s Administrative Offices and on the Palomar Health Development, Inc. (PHD) home page on the PH website on Tuesday, November 30, 2021, which is consistent with legal requirements. Notice of that posting was also made that date via email to the Board and staff members.
- As there was not yet a Chairperson, Director Griffith called the meeting to order at 11:03 a.m.
- Quorum was established (*see roster for attendees*)

**II. PUBLIC COMMENTS**

- There were no public comments

**III. INFORMATION ITEMS**

- None

**IV. OLD BUSINESS**

- None

**V. MINUTES**

**A. Minutes, Thursday, October 22, 2020**

**MOTION:** By Director Griffith, seconded by Director Greer and carried to approve the minutes from the Thursday, October 22, 2020, meeting  
Vote taken by roll call vote: Director Greer – Aye; Director Griffith – Aye

- Director Greer stated that she had read the minutes
- Mrs. Howell noted that – although Director Greer had not been on the Committee at the time of the meeting – it was appropriate for her to vote since she was now a member

**B. Minutes, Wednesday, September 15, 2021**

**MOTION:** By Director Greer, seconded by Director Griffith and carried to approve the minutes from the Wednesday, September 15, 2021, meeting  
Vote taken by roll call vote: Director Greer – Aye; Director Griffith – Aye

- Director Greer stated that she had also read this set of minutes
- Mrs. Howell noted that – although Director Greer had also not been on the Committee at the time of this meeting – it was also appropriate for her to vote since she was now a member

**HEALTH DEVELOPMENT SPECIAL AUDIT COMMITTEE – MEETING MINUTES – MONDAY, DECEMBER 6, 2021**

**(I.A) AGENDA ITEM**

**• DISCUSSION**

**CONCLUSIONS/ACTIONS**

**FOLLOW-UP/  
RESP PARTY**

**VI. NEW BUSINESS**

**A. Election of a Chairperson and a Vice-Chairperson of the Audit Committee**

**MOTION:** By Director Greer to nominate Director Griffith as the Chairperson of the Committee, accepted by Director Griffith  
 Vote taken by roll call vote: Director Greer – Aye; Director Griffith – Aye  
 No specific action was needed to elect Director Greer the Vice-Chairperson, as she is the only other member of the Committee

- Before moving to the next topic on the agenda, Director Greer asked if the other people in the meeting could be introduced
- Aimee Ebner introduced herself, stating that she is the accountant for PHD
- Jim Smith introduced himself as the VP of Finance for Palomar Health (PH), then stated that Ms. Ebner hadn't provided enough information about herself
  - Ms. Ebner has been an accountant with Palomar Health for about 12 years, she is technically very capable, and she is the member of the PH finance team who keeps all the books for PHD, with oversight from Sherray McCloud, Director of Finance for PH
  - Ms. Ebner does an outstanding job, both for audits as well as for the focused audits required as part of PHD's requirements under several grants

**VII. PRESENTATIONS**

**A. Audited Financial Statements – FYE June 30, 2021 – by Aldrich CPAs & Advisors LLP**

**MOTION:** By Director Greer, seconded by Director Griffith, and carried to recommend approval of the Audited Financial Statements – FYE June 30, 2021, as presented

- Mrs. Howell will forward the recommendation to the PHD Board at the December 13<sup>th</sup> meeting - ***DONE***

- Andy Maffia, Partner with Aldrich CPAs + Advisors, stated that he would be providing the results of the audit to this Committee, he would provide an opportunity for questions, and would present information regarding specific take-away points
- The documents were in draft form, on purpose: The Auditors had a chance to go over the draft with Management, and will do so with this Committee; then the final draft will go to the Board to ensure a fair and accurate picture has been presented, making sure that everyone has a good understanding of the documents
- As a non-profit, the audited financial statements will be available to the public, and the auditors felt that it was good for the members to know what the statements looked like and what was in them in order to be able to articulate that information to the general public should they be questioned
- Mr. Maffia asked that if at any point a Committee member had questions, they should feel free to ask them at that time, as he would be making an attempt to ensure that they as the Committee members were comfortable with the information
- EXECUTIVE SUMMARY (PAGE 21)
  - Provides the significant conclusions of the audit
  - Point one references the engagement letter that outlined Aldrich's responsibilities as the audit firm as well as the responsibilities of Management

**HEALTH DEVELOPMENT SPECIAL AUDIT COMMITTEE – MEETING MINUTES – MONDAY, DECEMBER 6, 2021**

**(I.A) AGENDA ITEM**

• DISCUSSION	CONCLUSIONS/ACTIONS	FOLLOW-UP/ RESP PARTY
<ul style="list-style-type: none"> <li>o At the end of the day, the auditor’s responsibility was to provide an opinion regarding PHD’s financial statements, which could be attached to the financial statements and would provide assurances as to the information the auditors were reviewing                             <ul style="list-style-type: none"> <li>– Basically reporting that a third party had reviewed and essentially given a stamp of approval to the information</li> </ul> </li> <li>o The opinion this year was an unmodified one – the highest level of assurance that could be provided                             <ul style="list-style-type: none"> <li>– It was the same opinion provided last year and for all the prior years for which Aldrich had been PHD’s auditor</li> <li>– Unmodified means there were no modifications to the standard report and, instead of saying, “everything was okay except for this...”, the report was clean and unchanged</li> </ul> </li> <li>o As the auditors reviewed information, they also looked at the internal controls within the organization, which are the checks and balances needed to help prevent and detect errors and prevent fraud                             <ul style="list-style-type: none"> <li>– The auditors then used that information to design their audit approach, in some instances testing controls and in others testing transactions</li> <li>– If areas of weakness or which could be strengthened were identified, that information would have been provided to Management; however, the auditors did not identify any material weaknesses or significant deficiencies</li> </ul> </li> <li>o The fourth bullet point speaks to the risk in how the audit is designed                             <ul style="list-style-type: none"> <li>– Since the auditors don’t look at every transaction that transpired throughout the year, they are sampling from populations as opposed to testing the whole population; and through that they narrow down the areas that need more significant testing than others, with the audit being designed with that approach in mind                                     <ul style="list-style-type: none"> <li>1) Through the information provided by the Management team, the auditors were then able to execute that plan</li> </ul> </li> </ul> </li> <li>o The final bullet point notes that the auditors received full cooperation from the Management team—VP of Finance for PH Jim Smith and Financial Services Manager for PHD Aimee Ebner providing the information                             <ul style="list-style-type: none"> <li>– Ms. Ebner was the primary contact, providing support to the auditors and answering their questions</li> <li>– Although it’s never fun going through an audit, the team was well prepared and extremely professional, providing all information needed to facilitate the work product in a timely manner</li> <li>– An audit can only be successful if Management is doing their job, and the outcome overall is a strong indicator of how the entire audit went, reflected in the unmodified opinion, with no lacks in internal controls, a testament that the entire team was taking their roles within the accounting function seriously</li> <li>– Mr. Maffia further noted that this was a report card for the Management team, and they did a tremendous job</li> </ul> </li> <li>• Director Griffith asked if any PH Board members had reached out directly to the auditors, and the answer was, “no”</li> <li>• Director Greer commented that Director Griffith had been on the PH Board for 10 years, and that she had been on the PH Board going on 16 years, they were both familiar with the audit process, and she thanked Mr. Maffia for letting them know that the team had been aboveboard and had helped rather than hindering them</li> <li>• INTERNAL CONTROL LETTER (PAGE 22)                             <ul style="list-style-type: none"> <li>o If deficiencies had been found, that information would have appeared within this letter; however, there were no material weaknesses identified</li> </ul> </li> <li>• AUDIT FINDINGS LETTER (PAGE 23)                             <ul style="list-style-type: none"> <li>o This is a required communication. internal both for Management and the Board, and it puts into writing what is being discussed today</li> </ul> </li> </ul>		



**HEALTH DEVELOPMENT SPECIAL AUDIT COMMITTEE – MEETING MINUTES – MONDAY, DECEMBER 6, 2021**

**(I.A) AGENDA ITEM**

**• DISCUSSION**

**CONCLUSIONS/ACTIONS**

**FOLLOW-UP/  
RESP PARTY**

- o If there had been any deficiencies, disagreements with Management, etc., that information would have been spelled out in this letter
- o The letter itself is overall fairly boilerplate regarding requirements
- o The paragraphs in the middle of the page identify that there are estimates built into the financial statements, which is not unique to PHD
  - All financial statements have estimates built into them, and this provides the opportunity to identify those estimates
  - There’s an estimate for the allowance for doubtful accounts, which is related to receivables
  - There were also estimates related to how expenses are allocated between program and supporting services
- SUMMARY OF ADJUSTMENT (PAGE 25)
  - o There was one adjustment, very insignificant in the grand scheme of this organization, but the auditors need to keep track of it in this package to ensure that the records on the audit side match those on the organization’s side
    - The adjustment was done in order for the financial records to match up with the audited financial statements from last year
    - Again, it was nothing uncommon, but keeping track of any adjustments needed to become a part of the package
    - Only having one adjustment was another strong indicator of how well the audit went; and, had there been several, it would have indicated there might need to be changes made to processes
- INDEPENDENT AUDITORS REPORT (PAGE 29)
  - o Mr. Maffia stated that the opinion rendered was an unmodified opinion, noting that the financial statements were presented fairly in all material aspects
  - o There was an emphasis regarding the economic dependency on PH, which had to do with negative amounts in net assets found on Page 30
    - If PHD had been a stand-alone entity, that could have triggered the reader to react negatively to the financials; however, knowledge of the relationship with the hospital would give the reader more comfort regarding the overall financial health of the organization
- Director Greer noted that PHD was a part of PH and PH was a part of them, and PH would support PHD just like they do any of the ACOs
  - o She further stated that PHD was managed well, and the grants had been very well-thought-out; however, she knew we had Forensic Health Services and the First 5 Commission grants, and she wondered if there was anything that listed those grants in this report
    - Mr. Maffia stated that nothing was required by GAAP regarding listing out the various grants
    - Mrs. Howell added that Ms. Ebner would be making a presentation on all the grants next week at the PHD Board meeting; and Ms. Ebner provided a brief rundown: First 5 Healthy Development Services provides occupational therapy for 0-5 kids; the home visiting program is funded by First 5 First Steps, Cal Learn and CalWORKs, and each grant provides the same type of services to various populations – home visiting for infants and new mothers; Forensic Health Services; Green Oaks Ranch intake center; and there is still a bioterrorism grant
- Mr. Maffia stated that the reason for having this meeting was to provide the opportunity for the Committee to ask those questions and to ensure that everyone had a good understanding of what was going on, then he asked if Director Griffith had any questions
  - o Director Griffith stated that there wasn’t anything that really stuck out to him, he thought Mr. Maffia had done a really good job with his overview, and it always made his year when the auditor declared that everything was good
- Director Greer asked for clarification about the process for providing this information to the PHD Board, and Mrs. Howell stated that the information would be forwarded as a recommendation from this Committee for next week’s Board meeting, at which time that body would review the materials and pass a resolution accepting the audited financials as the annual report of PHD

**HEALTH DEVELOPMENT SPECIAL AUDIT COMMITTEE – MEETING MINUTES – MONDAY, DECEMBER 6, 2021**

**(I.A) AGENDA ITEM**

• DISCUSSION	CONCLUSIONS/ACTIONS	FOLLOW-UP/ RESP PARTY
<ul style="list-style-type: none"> <li>o Mr. Maffia asked if he was requested to attend, and Mrs. Howell stated that 15 minutes had been allotted on the agenda just in case the members of the Board not on this Committee had any questions, so it would be appropriate for him to attend, and she would ensure that he had the invitation with virtual meeting information</li> </ul>		

**VIII. AUDIT COMMITTEE COMMENTS/FUTURE AGENDA ITEMS**

- None

**IX. ADJOURNMENT**

- The meeting was adjourned by Chair Griffith at 11:36 a.m.

**SIGNATURES:**

**PHD Board Audit  
Committee Chair**

\_\_\_\_\_  
Jeff Griffith, EMT-P

**PHD Board Audit  
Committee Assistant**

\_\_\_\_\_  
Tanya Howell

**Next Meeting: TBD based on the scheduled start of audit work for the FYE June 30, 2022, audit**

# ADDENDUM B

## Palomar Health Development, Inc.

Meeting with the Audit Committee and Management

Year Ended June 30, 2022

September 9, 2022

To the Audit Committee and Management  
Palomar Health Development, Inc.

Dear Committee Members and Management,

We are pleased to discuss with you our audit service plans for Palomar Health Development, Inc. (PHD) for the year ended June 30, 2022.

The purpose of this discussion is to provide you with the required communications regarding the auditor's responsibility, the scope of the audit, and the timing of the audit.

We would also like to discuss current year developments at PHD, as well as the risk factors, professional and regulatory changes, and other factors that will be included in our planning for the audit and that will impact the performance of our audit.

We welcome any questions or input you may have about this audit service plan. We look forward to working with you again this year and consider PHD to be an important client for our audit practice.

Very truly yours,



Andy Maffia, CPA  
Aldrich CPAs + Advisors LLP

## SCOPE OF SERVICES

We are engaged to audit the financial statements of Palomar Health Development (PHD) for the year ended June 30, 2022. Professional standards require that we provide you with the following information related to our audit.

### Our Responsibility under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter dated September 9, 2022, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

### Planned Scope, Timing of the Audit, and Other

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested.

Our audit will include obtaining an understanding of Palomar Health Development and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to Palomar Health Development or to acts by management or employees acting on behalf of Palomar Health Development. We will generally communicate our significant findings at the conclusion of the audit. However, some matters could be communicated sooner, particularly if significant difficulties are encountered during the audit where assistance is needed to overcome the difficulties or if the difficulties may lead to a modified opinion. We will also communicate any internal control related matters that are required to be communicated under professional standards.

Andy Maffia is the engagement partner and is responsible for supervising the engagement and signing the report or authorizing another individual to sign it.

This information is intended solely for the use of the board of directors and management. of Palomar Health Development and is not intended to be, and should not be, used by anyone other than these specified parties.

**SCOPE OF SERVICES, CONTINUED**

Our services include:

- ▶ Financial statement audit and opinion on PHD’s financial statements as of June 30, 2022.
- ▶ As considered necessary under professional standards, and based on our judgment, a management letter commenting upon the internal controls of PHD, fiscal management practices, and other observations resulting from the audit.
- ▶ A letter to the Board of Directors and Audit Committee, identifying significant accounting policies, management judgments and accounting estimates, audit adjustments and other matters discussed during the audit.
- ▶ Meetings with the Board of Directors and/or Audit Committee prior to and at the conclusion of the audit, and at other times, as deemed appropriate.
- ▶ Completion of the information returns (form 990)

**CLIENT SERVICE TEAM**

Aldrich uses a client service team to bring a broad range of competencies to our engagements. We will assign a client service team that will lead our services and the additional staff needed for your requirements. The client service team will include:

- ▶ Andy Maffia, Partner – Responsible for all professional services
- ▶ Shane Valleau, Senior – Responsible for managing day-to-day audit activities
- ▶ Rachelle Jumper, Manager – Responsible for the completion of the tax filings and tax consulting services

All members will be actively involved and available for the duration of the assigned services, and additional staff members will be assigned and available as needed. All staff have significant experience with not-for-profit organizations. Should there be any management staff changes we will discuss them with you prior to implementation.

**SERVICE TIMELINE**

We will work with management to determine a detailed timeline for our audit procedures. Our general timing is as follows:

Pre-audit meeting with the Audit Committee and management to obtain further understanding of PHD and develop a work plan, including discussion of the audit plan	September 9, 2022
All requested information to be provided to Aldrich	No later than September 12, 2022
All selections to management	No later than September 14, 2022
Selection documentation to Aldrich	No later than September 19, 2022
Complete fieldwork	Week of September 26, 2022
Delivery of audit report draft to PHD	TBD
Presentation of the audit results to the Audit Committee	TBD
Completion of the information returns (990)	TBD

## COMMITMENTS

Adhering to the agreed upon timeline will not only make the audit efficient, but it will allow us to meet your deadlines while minimizing the burden on your team. If there are delays in providing Aldrich the requested information on those dates, please connect with us immediately. We will work with your team to adjust the schedule which could include delays in performing audit procedures, adjusting the due date of the report, and/or additional fees.

## SIGNIFICANT AUDIT AREAS AND ISSUES

We will focus our audit efforts on the following significant areas:

- ▶ Cash
- ▶ Grants receivable
- ▶ Revenue recognition cycle
- ▶ Net asset restrictions
- ▶ Payroll and related liabilities
- ▶ Functional expense allocations
- ▶ Controls associated with significant transaction cycles, including revenues, expenditures, and payroll

## FRAUD CONSIDERATIONS

Our professional standards require us to consider the risk of fraud. As it relates to our audit, fraud includes the misappropriation of assets or fraudulent financial reporting. Procedures we will perform relating to fraud considerations include:

- ▶ Reviewing internal controls for susceptibility to fraud.
- ▶ Considering the control environment and pressures/incentives to commit fraud.
- ▶ Questioning employees at various levels within PHD regarding fraud.
- ▶ Our professional standards also require us to make inquiries of the board of directors, or a representative thereof, related to fraud concerns.

## PEER REVIEW

We have included our 2020 peer review report below for your records.

### Briscoe, Burke & Grigsby LLP CERTIFIED PUBLIC ACCOUNTANTS

#### Report on the Firm's System of Quality Control

October 5, 2020

To the Partners of Aldrich CPAs + Advisors LLP  
and the Oregon Society of CPAs

We have reviewed the system of quality control for the accounting and auditing practice of Aldrich CPAs + Advisors LLP (the firm) in effect for the year ended April 30, 2020. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants (Standards). A summary of the nature, objectives, scope, limitations of, and the procedures performed in a System Review as described in the Standards may be found at [www.aicpa.org/prsummary](http://www.aicpa.org/prsummary). The summary also includes an explanation of how engagements identified as not performed or reported in conformity with applicable professional standards, if any, are evaluated by a peer reviewer to determine a peer review rating.

#### Firm's Responsibility

The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. The firm is also responsible for evaluating actions to promptly remediate engagements deemed as not performed or reported in conformity with professional standards, when appropriate, and for remediating weaknesses in its system of quality control, if any.

#### Peer Reviewer's Responsibility

Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review.

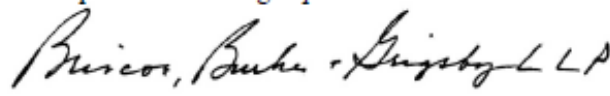
#### Required Selections and Considerations

Engagements selected for review included engagements performed under *Government Auditing Standards*, including compliance audits under the Single Audit Act and audits of employee benefit plans.

As a part of our peer review, we considered reviews by regulatory entities as communicated by the firm, if applicable, in determining the nature and extent of our procedures.

#### Opinion

In our opinion, the system of quality control for the accounting and auditing practice of Aldrich CPAs + Advisors LLP in effect for the year ended April 30, 2020, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of *pass*, *pass with deficiency(ies)* or *fail*. Aldrich CPAs + Advisors LLP has received a peer review rating of *pass*.

  
Certified Public Accountants

Members American Institute of Certified Public Accountants  
4120 East 51<sup>st</sup> Street Suite 100 Tulsa, Oklahoma 74135-3633 (918) 749-8337



## PROFESSIONAL AND REGULATORY CHANGES

The following items relate to changes throughout the not-for-profit environment for the benefit of the audit committee and management:

### State of Nonprofits

#### Technology

Flexible and remote working arrangements became essential to continued operations for many not-for-profits (NFPs) during the pandemic. Remote work presents unique challenges, particularly for information security controls, because remote work environments do not usually have the same safeguards as office environments. When employees are at the office, they typically work behind layers of preventive security controls. When computers leave the perimeter and people work remotely, new risks arise for the organization, and additional security policies are essential. According to the March 2020 Information Technology Laboratory Bulletin published by the National Institute of Standards and Technology, organizations should “plan telework-related security policies and controls based on the assumption that external environments contain hostile threats.”

Following are some information security and remote working best practices NFPs should consider when reviewing or developing policies and procedures:

- Establishing and communicating remote work security policies (for example, avoiding public wireless networks and use of personal devices or computers to store or process work information).
- Addressing authorization and authentication
- Ensuring employees are aware of current phishing and malware campaigns
- Securing communication channels
- Providing vigilant IT support
- Encrypting sensitive data

One of the most challenging issues arises as soon as assets are moved outside of an organization's physical office. Without proper foresight and the necessary tools, the IT environment can become difficult to manage and control. An organization may not know what information staff members are accessing, where they are accessing it, and what tools they are using to do so. Without managing this new remote freedom, the organization will undoubtedly experience the challenges associated with decentralization.

Data is arguably an organization's most important asset. The confidentiality, integrity, and availability of critical, sensitive, and proprietary data should be maintained. When data is housed solely on an internal network, implementing controls to protect that data is often more manageable. Organizations generally know where the data is, how it is accessed, and by whom.

However, with the move to more remote work, managing data becomes less straightforward. Staff members, typically without malicious intent, may implement various applications to increase their productivity or to fill a need that their IT department is not providing. However, this “shadow IT,” implemented by staff on their own, is concerning. If organizations do not know what technology staff are implementing, they cannot secure it, and depending on the nature of the implementation, the staff member could be unknowingly exposing organization data.

## PROFESSIONAL AND REGULATORY CHANGES, CONTINUED

### State of Nonprofits, continued

#### Technology, continued

Staff members who are not using organization-managed devices are even more concerning. Organization-owned devices are typically equipped to meet baseline security standards. However, personal devices may be unsecured from the start. The risk continues to grow if personal devices are shared among members of a staff member's household, such as children attending school virtually or family members using the device for recreational purposes. These individuals are likely less cognizant of malicious links on social media or in email, and the potential for inadvertent downloads of malware on the system increases. Organizations should define their expectations for the use of personal devices for work purposes.

Along the same lines, consider public wireless or home networks that staff members may be using to access organization resources. These environments further introduce unmanaged technology. Not only is there an increased risk of vulnerability from the actual internet source, but there is heightened concern with the other endpoints connected to it. Network resources could be shared with other unmanaged computers, printers, scanners, and various internet-connected smart devices (for example, smart TVs, alarms, thermostats, or refrigerators). If not properly secured or segmented, these other devices could affect the devices staff members use to access organization resources. Finally, many home-based smart devices listen for commands (for example, "Hey Alexa! What's the weather?"). To do this, these devices are "always on," which means they are always listening and sending the data to various data centers for processing. If a staff member regularly has sensitive, work-related conversations with a smart listening device nearby, then it is likely that these conversations are being recorded and stored, even if just temporarily.

#### Ransomware Threat

Cybersecurity has been a serious concern in both the public and private sectors for quite some time, but the stakes are rising as new types of threats emerge and organizations pivot to a more significant remote delivery model. Among the most pervasive of the current generation of threats is ransomware. In its most basic form, ransomware is malicious software that blocks access to a system or data until a sum of money is paid. However, variations exist that start destroying data until a ransom is paid or an attempt to obtain and exfiltrate sensitive information is made. Some ransomware variants, such as NetWalker, have evolved from broadly distributed attacks to more targeted attacks of specific organizations. Threats like these are not only more difficult to prevent, but they also are more malicious in their intent and devastating in their potential effects. Their consequences are often immediate and severely damaging.

Most security experts have come to recognize that cyberattackers have become more numerous, more persistent, and cunning enough to make incident prevention alone an inadequate strategy. Organizations also are recognizing the near certainty that some of the attackers' attempts will succeed. In other words, it's no longer a question of whether an attack will succeed, but when. What steps can an organization take to minimize the effects of an attack?

If your organization has concerns in this area or would like to have an external party review your security Aldrich Technology can help with this. Please talk to a member of your service team if you have questions.

## PROFESSIONAL AND REGULATORY CHANGES, CONTINUED

### State of Nonprofits, continued

#### Challenges with Resources

NFP revenue sources vary depending on the type of organization, ranging from membership dues to tuition to contributions and government grants. Yet, all these sources have been affected by the pandemic as special events have been canceled, schools have been closed, pledges have been uncollectible, membership dues have declined, and government funding sources have changed. Faced with the question of how to continue to provide services with less resources, organizations have re-forecasted their budgets to align with the changes happening due to the pandemic.

The risks associated with declining revenue can be both short and long term, and it is important for NFPs to consider the impacts on the financial viability of the organizations. NFPs with going concern issues have had to immediately assess their current situation, create financial scenario plans, and take strategic cost-saving measures. Many have had to discuss increases in spending from endowment funds and using board-designated funds to bridge the gap due to loss of operating revenues. Many organizations have approached donors to reclassify restricted funds for general operations.

NFPs that provide frontline services, such as health and human service organizations, have seen increased demand for their services during the pandemic. However, their ability to provide those services has been challenging due to various COVID-19 - related impacts, including significant numbers of staff who were sick, quarantined, or working remotely and the inability to obtain personal protective equipment in a timely manner. Several NFPs simply had to close certain programs because it was impractical or impossible to provide the services in the current environment.

#### Workforce

Because so many NFPs provide services as opposed to goods, remote working and employee safety have been key challenges. Many organizations were not set up for remote work at the onset of the pandemic (for example, they relied on systems that are not cloud-based or lacked sufficiently strong security controls) and have had difficulty transitioning. Flexibility and a focus on security and communication were critical.

NFPs that typically provide face-to-face services are challenged by staff who are reluctant to work in that type of environment. Workforce challenges also include staff retention and recruitment as budget cuts have affected compensation, benefits, and staffing plans. For those still hiring, recruitment and onboarding processes have had to be conducted remotely. NFPs that have maintained a thriving workforce during this crisis have kept a critical focus on their people, including health, safety, and well-being.

#### Internal Control

Remote work environments also have brought changes to systems of internal control. Remote work environments have required organizations to re-evaluate their internal control systems to make sure that the controls are still effective with the change in location and information sources in a remote environment. Many NFPs have had to reevaluate existing controls for unintended gaps and design and implement new or mitigating controls (for example, digital review and approvals). Updates to existing policies or creation of new policies have also been needed to accommodate adjustments in roles and responsibilities, new funding sources, changes in IT, and so on.

## PROFESSIONAL AND REGULATORY CHANGES, CONTINUED

### State of Nonprofits, continued

#### Internal Control, continued

Segregation of duties is often a challenge for small NFPs, but this challenge is magnified in the pandemic environment because of the changes in processes and duties necessitated by more virtual operations. With these changes, management will need to carefully consider who holds physical custody of assets, who is responsible for recordkeeping for assets, and who can authorize and approve transactions, and ensure those functions remain separate.

Documentation, although always important, may also require additional emphasis in the COVID-19 environment due to potentially increased scrutiny of estimates that affect key areas of the financial statements. Thorough explanations and supporting documentation for management estimates, including assumptions and methodologies applied, will be more important than ever given the heightened risk in areas such as asset impairment, debt covenants, and assessments of the entity's ability to continue as a going concern. Detailed recordkeeping also will be necessary for any COVID-19 - related funding received and related costs incurred.

Staff members will continue to welcome remote working arrangements for various reasons, and for many organizations, remote work is essential to continuing operations in the current environment. Organizations should adapt to this change by understanding the risks, potential security impact, and underlying implications for the financial statement audit if risks go unmitigated. Organizations should first measure their risk by defining who is working remotely and how and why they are accessing and storing data via applications, hardware, and other technology. Once this assessment is completed, controls can be enforced and monitored. Whether applied to cloud-based applications or virtual private network (VPN) solutions, authentication controls (for example, password, lockout, and multi-factor authentication), data loss prevention capabilities, and compliance monitoring are important.

#### New Audit Reports

For audits of December 31, 2021 and after there will be a new format and wording to the engagement letter and the audit reports that are issued due to the implementation of new auditing standards. These standards are intended to enhance the communication value and relevance of the reports.

The new audit report standards also include required procedures over annual reports. If your Organization issues an annual report that includes financial statement information or references the financial statements, there are required procedures that need to be conducted by your audit team. Your audit team will go over the specifics of these requirements.

#### New Standards for Presentation and Disclosure of Gifts-in-Kind

ASU No. 2020-07, Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets, issued in September 2020, requires new presentation and disclosure standards for gifts-in-kind. The new standards are effective for fiscal years beginning after June 15, 2021 (and for those who do interim reporting, interim periods beginning the following year). Gifts-in-kind, referred to as contributed nonfinancial assets, are items such as food, supplies, used clothing and household items, intangibles, medical equipment, pharmaceuticals, and contributed services. The following paragraphs discuss the new standards and review certain existing standards for estimating the fair value of gifts-in-kind.

## PROFESSIONAL AND REGULATORY CHANGES, CONTINUED

### State of Nonprofits, continued

#### New Standards for Presentation and Disclosure of Gifts-in-Kind, continued

Under ASU No. 2020-07, NFPs are required to present gifts-in-kind as a separate line item in the statement of activities, apart from contributions of cash and other financial assets. An NFP is required to disclose in the notes to financial statements the total value recognized for each category of gifts-in-kind received, the sum of which should agree to the total value of gifts-in-kind recognized in the statement of activities.

For each category of contributed nonfinancial assets, an NFP is required to disclose the following:

- Qualitative information about whether contributed nonfinancial assets were either monetized (that is, sold) or used during the reporting period. If used, a description of the programs or other activities in which those assets were used should be disclosed.
- The NFP's policy (if any) about monetizing, rather than using, contributed nonfinancial assets.
- A description of any donor-imposed restrictions associated with the contributed nonfinancial assets.
- A description of the valuation techniques and inputs used to arrive at a fair value measure used at initial recognition.

#### Lease Accounting

FASB issued ASU No. 2016-02 in February 2016. This standard replaces FASB ASC 840, which was more than 40 years old. With the goal of increasing comparability and transparency, the new leases standard essentially moves operating lease obligations from the footnotes to the statement of financial position. Prior to ASU No. 2016-02, lessees recognized only lease obligations (liabilities) and related assets for capital leases. This left financial statement users lacking valuable information regarding an NFP's true operating costs and often required them to conduct further analysis of footnote disclosures to ascertain the costs of operating leases.

Bringing operating leases onto the entity's statement of financial position could make a significant difference in the numbers that an organization is reporting. However, many lessees will be able to meet the new reporting and disclosure requirements using existing systems and processes, keeping additional costs of providing the required information at bay. ASU No. 2016-02 will be effective for NFPs for fiscal years beginning after December 15, 2021.