Practical Actions and Tips to Help Prepare for your AFS

Michigan Cannabis Regulatory Agency Education Session

December 4, 2025

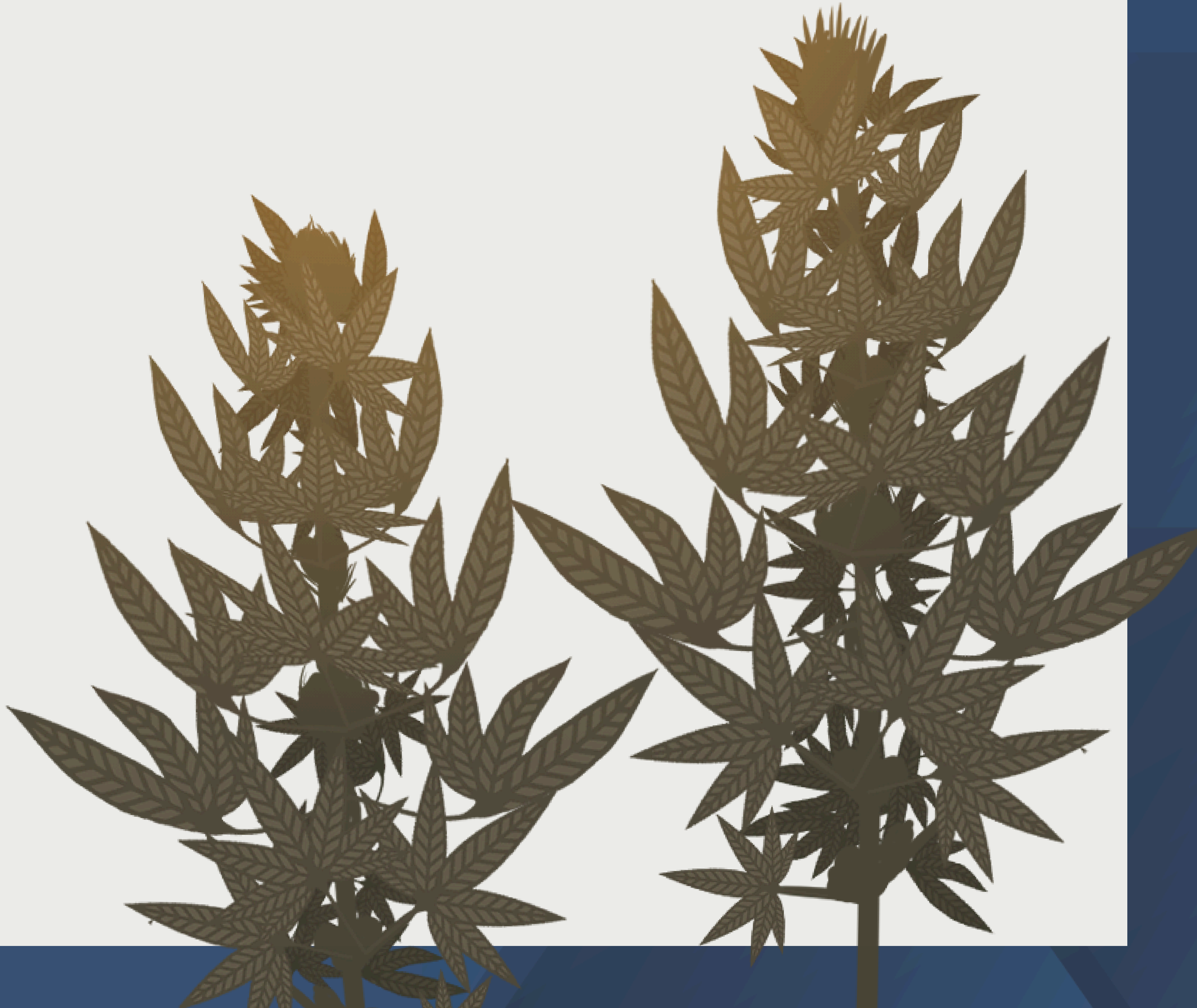
LEACIF

Accounting and Business Advisory

Why are we Presenting this Topic?

This presentation aims to help businesses better prepare for their AFS engagement and will provide actionable steps, tips, and resources that can help support a smoother process.

Why are we presenting this topic?



About the Presenter and Firm

Kareyna Miller, CPA, CRISC is a founding member of the MICPA Cannabis Industry Member Resource Group, and has been working with businesses in Michigan's cannabis industry since 2017. She has been involved in the AFS process from different perspectives, including first as a member of the workgroup to develop the initial procedures, and now in supporting and performing AFS engagements. Her industry experience includes accounting, tax, and attestation services.

LEACIF specializes in working with Michigan cannabis businesses for their accounting and business advisory needs, including controller, CFO, and tax services. The firm provides AFS report services for small and medium-sized businesses, and has developed its engagement process to support a smooth and efficient experience. Learn more at leacif.com/afs.

Disclaimer

The information provided herein is not and shall not be construed as AFS, tax, accounting, legal, regulatory or other professional advice or sufficient to satisfy any such requirements.

Attendees should consult AFS, tax, accounting, legal, regulatory or other professional advisor(s) for advice appropriate to their situations. This presentation is not sufficient to rely on and the information presented is not complete - many other matters affecting your business needs are also applicable.

This presentation is for general purposes only. Please consult your CPA regarding your specific business.

What is an AFS Engagement?

- Annual Financial Statement (AFS) engagement overview
- CPA completes the report form for the Licensee to submit
- Report form and instructions are available on the CRA's website at: https://www.michigan.gov/cra/sections/annual-financial-statements

Timing Your Engagement

Plan ahead and make sure your records ready.

- Expect to receive a notice of the report due date 6 months prior.
- As a best practice, engage a CPA to perform the AFS as early as possible.
  - The AFS period will cover the annual accounting period ended, generally just before receiving the notice.
- Reports due 12/31, have an AFS period of 7/1 - 6/30; Notice should arrive shortly after 6/30.
- **Ensure your books are closed timely and records are ready for the AFS process.**
- **Engage a CPA early: 3 months out is a general minimum; The earlier, the better!**

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Reconcile revenue for the AFS period
    - Retail: Reconcile revenue per METRC to Revenue per your General Ledger and Revenue per your Point of Sales System.
    - Cultivation and Processing: Reconcile "Received" revenue per METRC to Revenue per your General Ledger.
        - Reconcile revenue under tolling agreements
    - Secure Transport and Safety Compliance: Ensure all revenue sources are known and can be listed from largest to smallest.

- **Identify and document discrepancies**
    - Do not wait until the AFS to do this. There may be more discrepancies than anticipated.

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Identify and document discrepancies:
  - Discrepancies should be identified and documented by Manifest # or Sales Receipt #
- Discrepancies might include:
  - Errors from the POS transferring to METRC (test transactions, data entry errors, etc.)
  - $.01 transactions, Shipped but not Received transfers, data entry errors.
  - Non-METRC revenue, such as accessories or service revenue.
- Identify manifests or sales receipts with discrepancies, the amount of the discrepancies and reason for the discrepancies.

Best Practice: Reconcile revenue at least monthly. For example, as of today, December 4, 2025: are you confident your revenue is reconciled through October 31, 2025? If not, <u>why?</u>

Best Practice: Use different accounts in your chart of accounts to track discrepancies and Non METRC revenue.

Ensure Records Are Ready

Other Documentation Needed for Revenue Procedures:

- **Cash handling procedures:** Even if your business does not handle cash, ensure that written procedures are in place in case of this scenario. These procedures need to be documented in the AFS report.
    - Management's description should include, but not be limited to, how cash transactions are handled, how cash is stored (safe, deposit box, etc.), how cash is documented and reconciled, and how often reconciliations are performed.
- **Revenue reconciliation procedures:** Management's description should include, but not be limited to, how revenue recorded in the General Ledger, POS, and METRC is reconciled and how often reconciliations are performed.
- **Tolling/Service agreement reconciliation procedures**: Management's description should include, but not be limited to, how the revenue recorded in the General Ledger and Metrc is reconciled and how often reconciliations are performed, as well as how it is being manufactured if there is an agreement in place, and how the fees are determined.

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Identify (take an inventory of) all agreements currently in place:
  - Real Property Agreements
  - Financing Agreements
  - Management Agreements
  - Licensing Agreements
- Ensure each agreement is written
  - While agreements may be ‘verbal’, generally, a written agreement will need to be provided.
- Ensure appropriate agreements are reported to the CRA

Tip: If you are not sure which agreements are currently on file with the CRA, **ask**. For example, if you have a building lease agreement that has changed, ensure the correct copy has already been submitted to the CRA, before your AFS.

Ensure you are prepared to provide a complete and accurate list of agreements for the AFS.

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Reconcile payments under the agreement terms to your general ledger
    - For example, if a lease agreement is for $5,000 per month, have $60,000 in payments been made over the annual AFS period?
        - If not, why? An explanation will need to be provided.
        - If not, is an agreement in place to make up for the under or over payment(s)?
- Ensure that the parties to the agreements are correct
    - Do the parties’ names agree? For example, if the lease agreement is with Landlord Company LLC, are the payments being made to Landlord Company LLC?

Tip: If there are discrepancies, discuss these with the CPA performing the AFS, while the engagement is being scoped.

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Identify all vendors by their full legal names
- Prepare a list of all payments to vendors
  - The list should include payments only; not bills or other entries that do not represent payments out.
  - **Tip:** Multiple reports or formatting specific reports may be needed to accurately produce this list from your accounting system. For example running the 'Expenses by Vendor' report from QuickBooks Online will not include Bill Payments.
  - **Tip:** Ensure vendor payments are captured under the correct vendor, by legal entity. For example, if a vendor has an assumed name that operates under multiple legal entities.
- Ensure all expenditure transactions have a vendor associated
  - **Tip:** Review your general ledger for missing vendors and vendor reports for 'unspecified vendors'.

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Ensure transactions on credit cards or for reimbursements are captured correctly.
    - For example, if your business uses a credit card, the underlying transactions to the vendors must be identified and listed, not the bulk payments to the credit card company.
    - Payments for interest or card fees should be included separately and identified to the credit card vendor.
- Identify descriptions for each vendor, including their business purpose and what products or services they supply.

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Identify each vendor as a ‘Service’ or ‘Other’ vendor
  - **Best Practice:** Refer to AFS Instruction booklet for description of Service vs Other.
  - **Tip:** Discuss with CPA performing AFS during scoping or prior to providing vendor list if you are unsure of whether a vendor should be considered a Service or Other vendor. It is important to have this classification correct prior to samples being requested.
- Ensure documentation for vendor transactions is available. Appropriate documentation includes the vendor’s document, such as a receipt or invoice/bill.
  - **Tip:** Attach vendor receipts and other documents directly to the transaction in your accounting software.
  - **Tip:** If documentation is missing, reach out to the vendor to see if they can provide a new document copy.
- **Best Practice:** Document or discuss vendor payment procedures, including terms or payment cycles. For example, if your business commonly pays partial payments on vendor invoices, discuss this with the CPA performing the AFS during scoping.

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Prepare a report with detailed payroll information for each employee, including regular and bonus payments, pay rate information, and total payments during the AFS period
  - **Tip:** Identify if any employees were paid more than 10% of gross profit.
    - **Tip:** Understand the nature of your business and its gross profit and net profit. It may be that some employees are paid more than these amounts.
  - **Tip:** Identify if any employees received a bonus of more than 25% of their pre-bonus compensation.

- Ensure that bonus and stock option plans are documented.
  - **Question:** Does your business offer bonuses in the form of free products, or has it considered this? Is the documentation appropriate and payment value captured?

Ensure Records Are Ready

Think your records are ready for the AFS process? Can you:

- Confirm that the ownership structure that is currently in place is on file with the CRA
  - Ownership changes must be reported, including those that occur during the AFS period.
  - **Tip:** Ensure that operating agreements are kept up to date.
  - **Tip:** When considering changes to income tax structure, assess whether corporate documents need to be updated. Tax information is not covered in the AFS.
- Prepare a list of distributions to owners, including how the distributions were paid
  - **Tip:** Ensure that equity distributions are accurately recorded in your general ledger. For example, check for miscategorized payments to owners, such as for loan repayments or expense reimbursements, or payments recorded to an expense account that should have been recorded to an equity type account.
- Prepare a list of payments to ‘other persons’, or those whose payments were not included as an owner, employee, vendor, or under an agreement

General Documentation Requirements

- General Ledger:
  - **Tip:** Run your General Ledger report periodically and check for correctness and completeness.

- Financial Compliance Number: “FCR-XXXXXX”

- All documentation should be for the report period.
  - **Tip:** If gathering transactions from credit card statements, capture only the expenditure transactions to vendors that occured during the AFS period, even if the credit card statement dates align differently.

- Make sure all requested information and documents are accurate and complete before being provided to the CPA performing the AFS.

Revenue Procedures

Documentation to gather:

- Retailers: METRC Sales Transactions Report* or Monthly Sales Report
  - *The AFS instructions request the Sales Transactions Report; However this report often will not generate from METRC, due to the amount of data.
- Cultivators and Processors: METRC Wholesale Transfers Report
- Revenue for secure transporters and safety compliance facilities is tested differently, since revenue transactions for these types of businesses are not reported in METRC.
  - A sample of sales invoices will be required for revenue testing.

Agreement Procedures

Agreements to gather include:

- Real Property Agreements - Building rental agreements or land contracts, including agreements that expired during the report period and amendments.
  - Square footage of the property is also requested.

- Financing Agreements - Loans with individuals who are not supplemental applicants or a registered financial institution.

- Management Agreements - Agreements for others to perform management services or duties for the business.

- Licensing Agreements - Agreements to operate within or produce for another Licensee’s space or brand.

Tips Before Submitting Agreements

- Review agreement terms. Trace monthly payments to the general ledger to ensure they are taking place accordingly.

- If there are differences, ensure an explanation is prepared and any related support documentation is also provided.
  - Why was the amount per the agreement not paid? Is there an agreement to make up the additional difference (or address an overpayment)?

- Ensure agreements are up to date with the CRA, including any changes. Reported agreements should be submitted with the AFS report if they are not already on file.

Service and Other Vendors

- **Provide a list of vendor payment transactions for the reporting period.**
  - Ensure payments are listed under the correct legal entity name for all vendors, as registered with LARA or otherwise.
- Service Vendors - Intangible services, such as utilities, supply chain financing, transport services, insurance, etc.
- Other Vendors - Includes inventory purchases, supplies, and materials, etc.
- Full descriptions of both types of vendors are included in the AFS instructions and report form.
- Vendor types must be identified correctly so that vendors are accurately reported and sampled.

Vendor Transactions

- Vendors will be ranked by the total amount paid to them during the report period.
  - All reports require the Top 20 Service vendors to be reported.
  - Depending on the number of licenses your business has, up to 30 Other vendors may be reported.

- Based on their type (Service or Other), vendors are sampled in accordance with the instructions.
  - 3 or more licenses will require the maximum amount of vendors to be reported and sampled.

- Support documentation will be requested for vendor transactions that are selected for sampling.
  - Source Documents should come directly from the vendor. Checks and bank statements are generally not acceptable support documentation.

Vendor Sample Best Practices

- Provide complete documents. If the vendor’s invoice is 15 pages, provide all 15 pages.

- Redact any sensitive information, such as bank account and credit card numbers.
  - **Tip:** Take care that your vendor’s data is not inadvertently exposed.

- Ensure timeliness; The Licensee will need adequate time to gather the support documentation, and the CPA will need adequate time to review, document the details, and complete any findings on the report. Follow-up questions and other ‘back and forth’ should also be anticipated.
  - The vendor procedures typically take the longest to complete.
  - **Tip:** Anticipate 3-4 weeks for the vendor procedures to take place, or longer depending on sample volume.

Ownership and Other Persons Procedures

- For the Ownership procedure, businesses will need to provide:
  - Ownership agreements in place during the AFS period, including amendments.
  - List of disbursements to owners through equity, and how the disbursements were paid.
  - Ensure that ownership is correctly updated and reported to the CRA.
- Other Persons Procedure - Confirm if there is anyone not previously identified under the Ownership or Employee procedures who received 10% or more of the business's revenue or profit.

Employee Procedure

- Documentation to provide includes:
  - Payroll journal, broken out by employee and the types of payments made to them.
  - Breakdown of normal salaries and wages paid vs. bonuses.
  - Copies of any bonus and employee stock option plans.
  - Separate identification of any employees who are paid 10% or more of the business's profit, and who received a bonus of 25% or more of their pre-bonus annual compensation.

Due Diligence on Selecting an AFS Provider

- The CPA performing the procedure must be independent according to professional standards. Clients can implement safeguards to help ensure independence requirements are met.
    - **Tip:** Providing accounting services for a business often makes the CPA not independent. If you work with the AFS provider for accounting or other non-attest services, inquire to understand the CPA's due diligence procedures to ensure independence standards are met.
    - The CPA should not assume management functions of the Licensee during the AFS process.
- **Tip:** The CPA <u>should not</u> ask you to complete any part of the report or its schedules.
- Ensure engagement timing is appropriate:
    - **Tip:** 3 months is the minimum, ideally. 4 or 5 months are better.
- Use the Peer Review Public Search to ensure the CPA firm is enrolled in Peer Review.
- Be aware of the professional standards (the rules) the CPA should follow during the engagement.
    - AT-C 105, AT-C 215, SQMS, ET, and Michigan Accountancy Occupational Code.

Data Security Best Practices

- Ensure financial and other private business information is transferred securely.
  - **Tip:** Use a dedicated secure document sharing portal. If emailing sensitive documents, ensure they are password-protected.
  - **Tip:** If using a free or public file-sharing portal, review the vendor's data privacy and security policies to ensure information is kept secure.

- Ensure your vendors' information is not exposed.
  - **Tip:** Before submitting samples, review for and redact sensitive information. For example, vendors may provide their bank information on invoices for payment.
  - **Tip:** Consider including in your agreements with vendors that their information may be provided to a third-party for the AFS.

- Ensure your AFS provider provides their privacy policies to you.
  - **Tip:** CPAs are required to have certain data security measures in place. Don't be hesitant to ask about and discuss these.

Before Report Submission

- Review the report draft thoroughly before approval to make sure all the information is in the report and correct.
  - **Tip:** Ensure agreements are reported correctly, and none were missed.
  - **Tip:** Review AT-C 215 for guidance on how findings should be reported. Ensure none are stated as a ‘conclusion’ or contain words like ‘we do not consider’.
- Provide a Management Representation letter for the CPA to sign to confirm the information provided for the report.
- **Once the report is signed by the CPA, the process to reissue can require several steps and a new engagement letter.**

Resources & Any Questions?

CRA's AFS Section - https://www.michigan.gov/cra/sections/annual-financial-statements

- Includes AFS reporting schedule, Reporting instructions, support forms and more.

Peer Review Public Search - https://peerreview.aicpa.org/public_file_search.html

AICPA Ethics Library: https://pub.aicpa.org/codeofconduct/EthicsDevLogin.aspx

LEACIF AFS Resource - https://www.leacif.com/recent-publications/preparing-for-your-afs

Thank you!

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