



Verification Commission

Report to the 2021 General Assembly on the 2020 Financial Statements

The Verification Commission met via Zoom with the Ernest and Young auditors. All members were present.

The Commission then met in Moscow 30-31 July 2021. Members present in person were Chair Lakhdar Mazouz, Rajai Alsusi, and Allen Priest. Joining via Zoom for the whole meeting was Margaret Murphy. Joining via Zoom for a limited time was Panu Laine. (Referred to as VER) Others present in person from FIDE were Alexander Volzhin, Zhu Chen, and Willy Iclicki. Also joining via Zoom was Igor Kogan (referred to as FIDE Team).

Finally, the Commission met via Zoom in preparation for the General Assembly meeting in December 2021.

1- JUNE ZOOM MEETING

The Commission met in June with the Ernst and Young auditors (referred to as E&Y) via Zoom. The Commission members were able to ask the E&Y questions. E&Y issued an unqualified opinion. That is often called a “clean opinion” and is what you want the auditors to find. It means they found no uncorrected material errors. This does not mean the financial statements are perfect. It does mean readers should be able to draw the same conclusions about the financial statements that are presented as they would if the statements were perfect.

One thing we noted is that much of the audit staff changed from the prior year. It appears only the partner was the same from the 2019 audit. We addressed concerns with the timing of the audit to E&Y. The audit work did not start on time in accordance with their schedule in the arrangement letter. They also did not complete the work when they had contracted to do so. This delay meant the commission had to delay its work as well. However, due to the delays in the GA meeting dates because of the COVID, The VER will be able to complete its work in time. But in a normal year these delays are unacceptable. We expressed those concerns to the E&Y partner in charge of the engagement.

We did have the financial statements and the detailed support for several weeks to prepare for the Moscow meeting.

2- AUGUST MOSCOW MEETING

To open our meeting the FIDE team gave a summary of the financial statements for 2020. There were no changes between the time we met with the E&Y and the final statements upon which they issued their opinion.

The FIDE team stressed the problems with the timing of the audit work. They asked for the Commission's support to explore changes in the auditors to get a better response. We discussed a better choice might be an international firm a bit smaller than one of the "Big 4". The VER hopes FIDE might be a more important client to a smaller firm.

We did note the auditor said some of their delays were related to issues with contracts only being in Russian rather than in English, which is the official business language of FIDE. The auditor said they sent contracts to their Moscow office for translation which contributed to the delay. The FIDE team indicated they have asked for contracts to be in English, although there is an issue with getting Russian governmental agencies to agree to English language contracts. Still, we recommend FIDE prepare English versions or parallel dual language versions of all contracts.

We noted the amounts due to FIDE from Federations had declined significantly. While part of this may be due to the decline in activity related to COVID, the FIDE team noted the organization had implemented several changes to improve collections. First, there has been a concentrated effort to get debtor federations at least on a payment plan to start reducing the arrears. The FIDE team reported that Iran has now paid about half its total, Serbia is making payments with a goal of paying all its amounts by the end of 2023, and Mexico is now fully paid. There are still issues with balances due from Algeria, Venezuela, and Egypt, among others.

Second, there has been a change in billing practice to make it clear what the national federation agrees to have billed to the federation account. This has been an issue with certain federations who claimed amounts should have been billed directly to individuals.

We asked about the development of the nepotism policy as we had recommended last year. Such a policy is still in development. The FIDE team reported there are no FIDE employees who are direct reports to family members, so it appears there would be no violation of most standard nepotism policies.

The staff levels in 2020 are about the same as 2019 and the FIDE team reported the list of the FIDE staff we received late in 2020 was the same at year end. In 2021 there were several changes in roles and the addition of 3 positions to work with sponsors and development. This did not impact the 2020 audited financial statements.

There was a new bank added so the organization would have an account in Switzerland. We noted bank charges had returned to about the same amounts as in the years prior to the FIDE banking problems. E&Y noted, and the FIDE team confirmed, there are problems getting distributions from the PayPal account to the bank accounts. The issue with the PayPal account appears to be the account was established with the personal credentials of prior FIDE employees and is linked to a bank account which has been closed. While the staff reports some progress has been made, getting the account changed has been difficult and unsuccessful to date.

The auditors noted an issue with the Swiss Value Added Tax (VAT). It appears there has been a change in Swiss law. While small non-profit organizations were previously not required to file these returns, the law changed several years ago. According to E&Y there is no penalty under Swiss law for filing these

returns late, and FIDE would be eligible to receive refunds of some VAT previously paid. According to the FIDE team, FIDE will need to engage an outside agent to prepare the proper returns.

The auditor reported there were no major changes or releases of any excess reserves under Swiss law. Our review of the audited financial statements and the auditors statutory report supports that claim.

The auditor mentioned an issue with the revenue recognition policy. We discussed this at length with the FIDE team. Certain sponsor contracts are for specific events. The revenue from these is recognized when the event is held. That policy is not in question. However, certain other contracts have provisions for FIDE to generally publicize the sponsor. These, or similar, contracts have been extant in prior years, and the policy has been to recognize the revenue when the contract is finalized. E&Y did not raise any questions about this policy in prior years. But in 2020 E&Y required the contract revenue from these contracts to be spread over the contract period due to the publicity provisions. The auditor said this is because Swiss accounting standards emphasize form over substance. E&Y indicated the way FIDE was recognizing revenue would be in accordance with International Financial Reporting Standards which emphasizes substance over form in transactional reporting.

The FIDE team considered, and the Commission supported, changing contract terms to assign minimal amounts to the general publicity provision and explicitly state most revenue could be recognized immediately. This would be in keeping with prior practice and would satisfy the auditors' insistence that Swiss accounting standards emphasize form over substance by assigning the revenue to the various contract provisions.

The VER raised several questions about a new program which is called "Chess in Business" in the financial statements. The FIDE team description of the program is the development of a chess center in the geographic area of Russian high technology companies. The program was funded by a grant from a sponsor. The stated benefit to FIDE is visibility to these companies and their employees to spur further development of funding and sponsorships for FIDE. FIDE considers the program as an investment in its development strategy. While the program started in January 2020, the VER did not receive any indication if any new sponsorship has yet developed through the program, although we recognize the development process takes time.

3- PRIOR YEAR RECOMMENDATIONS AND RESPONSES

The VER reviewed our 2019 recommendations with FIDE staff. Most had been completed or adopted. The specific recommendations from the VER report on the 2019 financial statements and the FIDE responses are listed below.

Recommendation 1. FIDE should continue to make its financial statements in accordance with Swiss accounting standards and engage the audit firm to conduct a full scope independent audit as it has done for 2018 and 2019. The limited scope audit and the presentation of financial statements under FIDE's own accounting rules as was done prior to 2018 does not provide adequate assurance as to FIDE accounts.

Response 1. The 2020 financial statements were made in accordance with Swiss statutory accounting standards. The audit firm conducted a full scope audit for 2020.

Recommendation 2. A cash flow statement made under the indirect method was added to the FIDE internal financial statements in accordance with our prior recommendation. This should be included in the audited financial statement for 2020. (We understand management has already discussed this

increase in scope with the audit firm). We recommend preparing this statement using the direct method. The direct method lists details of the sources and uses of funds. While using this method will take additional time, it will provide better information to FIDE financial statement users. Since FIDE is a relatively small organization, the direct method will not be as much of an additional challenge as it can be for larger, more complex organizations.

Response 2. The cash flow statement was not included in the audited financial statement for 2020 because the contract with the auditor had been established before the VER recommendation was made. The internal financial statement included a cash flow statement prepared on the indirect method.

Recommendation 3. We support management's efforts to replace the custom Greek accounting program with a more standard commercial program. Such an accounting program should employ standard double entry accounting. The number of users who can post transactions to the accounts should be limited. But financial information should be widely available. Managers need financial information to be properly held accountable for financial results. Member federations and other interested parties need access to financial information to determine the effectiveness of FIDE management. And donors increasingly insist on financial information, so they know their donations are being properly spent.

Response 3. Due to the lack of time remaining in the year after the recommendation was made, this was not adopted. The FIDE team indicated a change in the accounting program is planned.

Recommendation 4. The auditor raised a question about proper documentation of expenses. It is critical for management to enforce internal control rules for adequate documentation of expenses. FIDE should refuse to reimburse expenses for anyone who does not provide adequate details until they comply with the documentation rules. Expense reports should all be approved by someone else – even expense reports of the President.

Response 4. All expense reports, including those of the President, are now being approved.

Recommendation 5. The Planning and Development Commission seems to have robust grant requirements. Those requirements and the application process, as well as the forms for the documentation of program results, should be easily available on the FIDE website.

Response 5. The grant requirements, applications and forms have been added to the FIDE website.

Recommendation 6. In the interest of transparency, development grants made should also be posted to the FIDE website.

Response 6. Grants made have been listed on the FIDE website.

Recommendation 7. The audited financial statement reports should be posted separately to the FIDE website. While they may be included as annexes to the FIDE General Assembly material, this can be hard for users to find.

Response 7. Audited FIDE financial statements for the last ten years have been posted to the FIDE website.

Recommendation 8. FIDE should not administer restricted grants that are received for the benefit of specific individuals or organizations. In the future FIDE should only accept grants for which FIDE can determine the recipients. As there are contractual obligations for the present arrangement, we believe FIDE must continue to administer the arrangement.

Response 8. FIDE continues to administer all ongoing contracts but has adopted a policy to not accept future grants that are restricted to the benefit of specific individuals or organizations.

4- CURRENT YEAR RECOMMENDATIONS

Our recommendations related to the 2020 financial statements are:

Recommendation 1. While we noted a cash flow statement prepared on the indirect method had been included in the internal statements, we again recommend the cash flow statement should be prepared on the direct method. While the direct method would take more time to prepare, it would provide more information to the financial statement users.

Recommendation 2. The auditor engagement should be expanded to include the cash flow statement.

Recommendation 3. The contract with the auditor must clearly state the audit must be completed by the end of May so the VER will have adequate time to complete its work.

Recommendation 4. The VER agrees with the FIDE team recommendation to explore a change in auditor. The purpose of the change is to find a firm that will have value the relationship enough to complete the audit within the time agreed to in the engagement letter.

Recommendation 5. The FIDE Charter states the business language of FIDE is English. Therefore, all FIDE contracts should be prepared either in English, or as a parallel dual language version.

Recommendation 6. As we previously recommended, FIDE should complete the development of a nepotism policy to clarify that any family members will not be in a supervisory position over another.

Recommendation 7. The resolution of the issue with access to the PayPal account funds needs to be a high priority.

Recommendation 8. FIDE needs to complete all required Swiss VAT returns and claim the appropriate refunds as soon as possible.

Recommendation 9. Future contracts for event or program sponsorships and general donations should include language to allocate contract revenue to the various requirements for FIDE to provide services. This will meet the requirements of Swiss statutory accounting rules while maintaining the customary revenue recognition policies of FIDE.

Definitions:

Restricted grants – funds provided by an organization to FIDE that stipulates exactly how it will be spent. Unless the funds are spent as stipulated, they must be returned to the grantor.

Sponsorships – funds provided to support a specific FIDE event or program in exchange for publicity before, during and after the event or program.

Donations – funds provided to support FIDE not connected to any specific event with little or no expectation of much publicity or restrictions on the use of the funds.

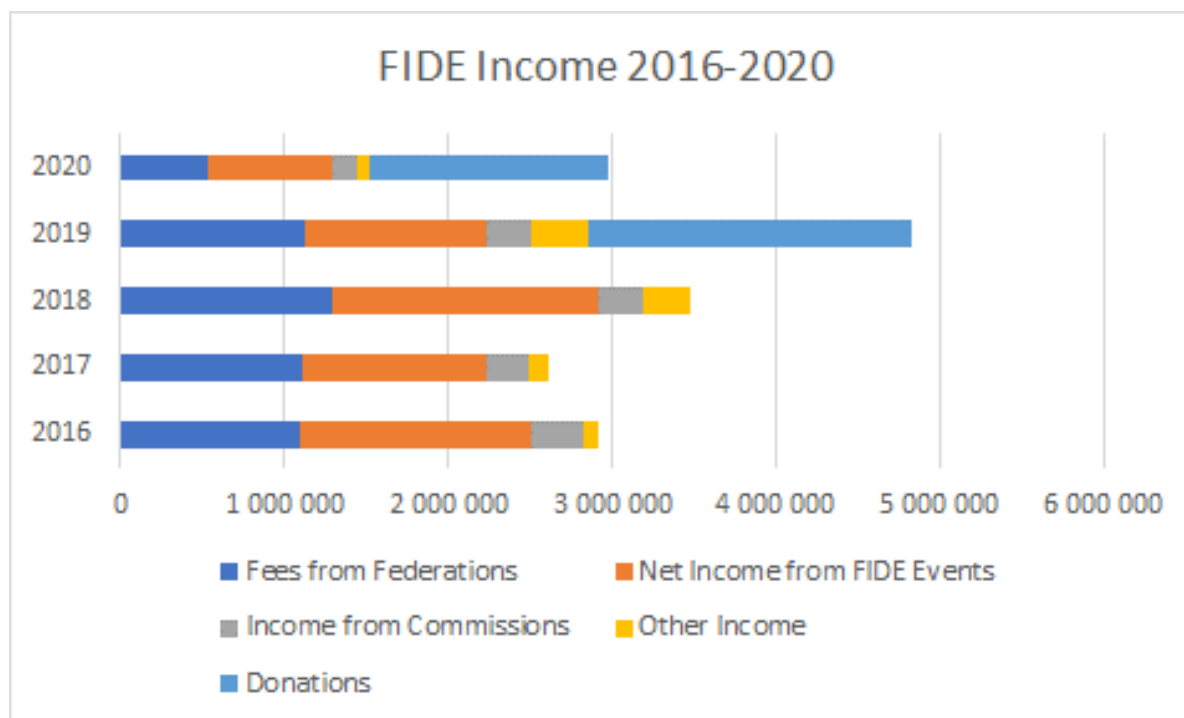
5- Trends of FIDE income/expenses

The VER met also on its own through a Zoom conference and commented on the trend of income/expenses since 2016 to 2020. (All figures are expressed in Euro)

INCOME					
	2016	2017	2018	2019	2020
Fees from Federations	1 098 327	1 112 442	1 295 302	1 123 810	539 025
Net Income from FIDE Events	1 411 315	1 116 372	1 616 902	1 112 468	757 373
Income from Commissions	309 142	260 582	275 345	275 257	146 824
Other Income	92 110	126 345	286 582	340 633	69 946
Donations	0	0	0	1 981 656	1 469 083
	2 910 894	2 615 741	3 474 131	4 833 824	2 982 251
EXPENSES					
	2016	2017	2018	2019	2020
Officials' expenses	176 911	247 558	629 186	366 639	73 731
Secretariat / All	671 881	613 810	676 521	1 001 577	1 010 178
General expenses	565 568	784 270	1 127 392	958 142	845 426
Commissions & Committees	618 885	422 741	675 971	443 657	277 847
Event Expenses	60 046	83 662	376 167	483 256	149 913
FIDE Development Fund				1 893 213	818 725
	2 093 291	2 152 041	3 482 237	5 146 484	3 175 820

- Development funds existed also in the years before. They consisted of funds provided for the Development Commission and Activity rebate. (See financial statements for the years 2016, 2017 and 2018). They amounted respectively to 220 570, 183 393, and 300 040.

5.1- Income



Income consists of:

1. **Fees from Federations** - mostly membership fees, entry fees, registered tournaments, change of federation's fees, title fees.
2. **Net Income from FIDE Events** - income from events like World Championship Matches, Candidates, Online events, World Cup etc.
3. **Income from Commissions** - Various seminar and license fees, up to Event Bidding Fees
4. **Other Income** - Various income, e.g., International Olympic Committee, rental of boards, interest from bank, royalties, etc.
5. **Donations** - Donations and sponsorship.

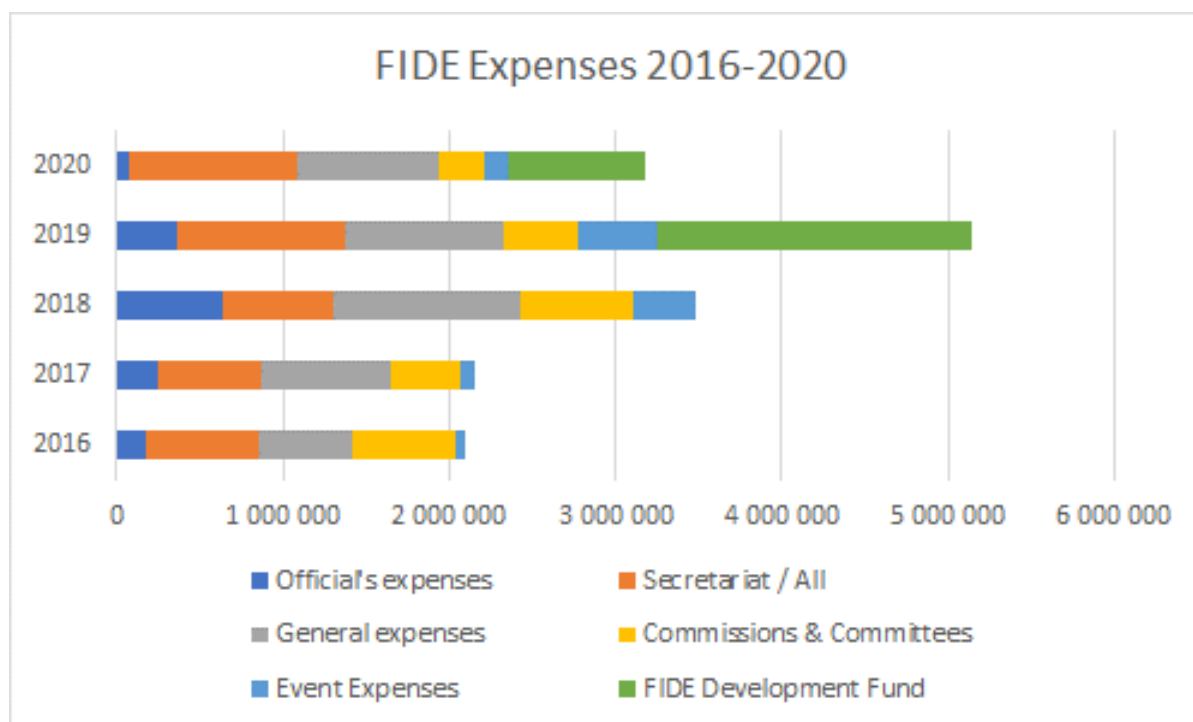
If one looks at the figures and at the Chart, one can see that the overall income has been about the same in 2016 and 2020 (respectively 2 910 894 and 2 982 251).

However, this is misleading if we compare only the total income. The COVID pandemic caused a large drop in the income derived directly from FIDE Chess activities. The decrease was 41% in a single year whereas donations decreased by 25.8%. With these changes, donations represented about half of the total income of FIDE.

The makeup of FIDE income has changed. In 2016, income from Federations, chess events and commissions represented 96.8% of the total. But in 2020, it represented only 48.3%. At the same time Income from donations and sponsorships constituted almost half of FIDE total income. In the absence of donations and sponsorship, as before 2020/2019, the impact of COVID would have crippled FIDE with financial problems. This is a turning point in FIDE policy which emphasizes, from now on, on developing more revenue outside its traditional income, thus avoiding depending on them. It is clear now that FIDE

should continue to look for new resources to realize its ambitions for sustained worldwide chess activities. No effort should be spared towards this goal.

5.2- Expenses



FIDE expenses consist of:

1. **Official's expenses** - Mostly Official's travel costs, Treasurer expenses, President advisers, council, and congress meetings.
2. **Secretariat costs** - Mainly of secretariat expenses in Lausanne/Athens and Moscow/Elista – (staff salaries & costs), office rent & costs.
3. **General expenses** - Mainly costs related to accountancy, audits, professional services, bank charges, currency conversion, depreciations, press/PR/marketing, taxes.
4. **Commissions & Committees** - Costs of various Commissions and Committees (20 Commissions in total in 2020) mostly for meetings and travel.
5. **Event expenses** - Varies a lot year by year. Includes World Championship matches, Olympiad, World Cup, various team events, electronic boards.
6. **FIDE Development Fund** - Development Fund for the 4 Continental Associations, for National Chess Federations and Social Projects and Reserves.

All item expenses, except Secretariat and general expenses which are basically fixed costs, have been affected by the COVID pandemic. Fewer chess activities meant reduced revenue but also fewer expenses.

Compared to 2019, expenses were cut by 38.3 % in 2020.

The development fund has been the most affected expense item. In 2020 Development fund expenditures decreased from 1 893 213 to 818 725, a decline of 56.7 %).

Expenses devoted to development represented 36.7% of total expenses in 2019, whereas they were 25.7% of the same total in 2020. Nevertheless, they are still a major component of FIDE costs.

However, note that in 2016, 2017 and 2018, development expenses represented respectively only 10.5%, 8.5% and 8.6% of total costs. This means FIDE has been recently multiplying efforts for chess development around the world.

6- DECEMBER ZOOM MEETING

As is customary, the Commission met on 22 December 2021 in preparation for the General Assembly. The Commission meeting was held via Zoom due to the pandemic. All Commission members were present. Others were invited to join the Zoom meeting. Attendees included several FIDE staff members as technical support as well as FIDE financial advisor Alexander Volzhin, FIDE Treasurer Chen Zu, FIDE special representative Willy Ilicki, FIDE legal counsel Aleksander Martynov, FIDE accountant Evangelia Perissiou and representatives of various Federations and Commissions including Ali Nihat Yazici, Lewis Ncube, Nick Faulks, Alex Holowczak, Jamie Kenmure, Allan Herbert, and Norlan Gaitan.

The agenda included a discussion of the FIDE audit process, a review of the auditors' report on the financial statements and their statutory report (management letter), comments by the Commission on the 2020 FIDE financial statements along with trends of FIDE income and expenses over the last five years, and a review of the Commission's recommendations.

The Commission took questions from the audience, most of the which were directed to FIDE financial officials who were present. The final report was amended to correct some minor drafting errors and to include the Commission's 2020 recommendations which had been inadvertently excluded from the draft report.