UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
CLOSE THE BOOKS

Control practices

The following control objectives provide a basis for strengthening your control environment for the process of closing the books. When you select an objective, you will access a list of the associated business risks and control practices. That information can serve as a checklist when you begin reviewing the strength of your current process controls.

This business risk and control information can help you assess your internal control environment and assist with the design and implementation of internal controls. Please note that this information is at the generic business process level and many companies will need to go beyond generic models to address the specific business processes that support the financial and nonfinancial disclosures being made. You can combine the insight of this business risk and control information with your industry-specific knowledge and understanding of your company's environment when conducting internal control assessments and designing and implementing recommendations.

Effectiveness and efficiency of operations

A. Cycle time is reduced.
B. Quality within the closing process is improved.
C. Employees and management are given the information they need to control the closing process.
D. Relevant management information is provided on a timely basis.

Reliability of financial reporting

A. Journal entries are properly authorized.
B. Journal entries are accurately and completely recorded on a timely basis.
C. Journal entries are reliably processed and reported.
D. Recorded balances are substantiated.
E. Recorded balances are evaluated.
F. All necessary reconciliations are complete and accurate.
G. Performance measures used to improve the process are reliable.

Effectiveness and efficiency of operations

A. Cycle time is reduced.

Business risks

- Information will lose its relevance for decision making because it is not generated on a timely basis.
- Excessive time and resources will be allocated to producing data and analyzing details. Creating information and insights through analysis will be neglected.
- A long closing process will increase employee workloads, leading to higher overtime costs and lower employee morale.

Control practices

1. Map the closing process to gain an understanding of key inputs, activities, and outputs.
2. Streamline the closing process to the extent possible.
3. Automate all manually produced, recurring entries where possible.
4. Perform all entries and activities that can be performed during the month outside of the closing "crunch."
5. Analyze the reasons and root causes behind errors.
6. Perform account analyses throughout the month to reduce month-end work.
7. Use standard and integrated information systems across all divisions and subsidiaries.
8. Consider quarterly closings and use of "soft closes" during the months regulatory closes are not required.

B. Quality within the closing process is improved.

Business risks

- Frequent errors will delay the production of required financial reports and lead to higher costs.
- Frequent errors will create a greater risk of errors remaining undetected after the process is completed.
- More general ledger passes will increase costs.

Control practices

1. Track errors in the process of closing the books, and create error reports to prevent future errors.
2. Use relevant performance measures to track improvements in the quality of the closing process and include days to close the books and error rates.

C. Employees and management are given the information they need to control the closing process.

Business risks

- Information provided to employees and management about the closing process will conflict with company objectives.
- Employee performance will not improve the closing process on a timely basis.
- Plans to improve the closing process will be based on incorrect perceptions of process performance.

Control practices

1. Align relevant performance measures with company objectives.
2. Prepare accounting personnel so they understand management and user expectations in relation to the quality and timing of information and reports from the closing process.
3. Compress cycle time for closing to the shortest time allowable.
4. Develop quantifiable and controllable performance measures that link the closing process to company goals and objectives and to management and user expectations to stimulate continuous improvement.

D. Relevant management information is provided on a timely basis.

Business risks

- Information used to support business decisions will not be relevant.
- Users and managers will make poor decisions because the information they use will be incomplete, out-of-date, or irrelevant to their decisions.
- Performance measures will not align with company objectives and will encourage actions that are inconsistent with those objectives.
- Performance measures and other information decision makers use to monitor the closing process will be irrelevant unless they align their requests for information with company objectives.
- The information process will be data rich and information poor unless available data is synthesized, summarized, and reported to the proper people in a form that supports decision-making.

Control practices

1. Report performance measures at predefined times and in standard formats.
2. Ensure that recipients of performance measure results understand the relevance of the measures.
3. Select performance measures that stimulate learning and process improvement.

Reliability of financial reporting

A. Journal entries are properly authorized.

Business risks

- Unauthorized or invalid entries will be recorded in the general ledger.

Control practices

1. Devise computer routines that automate recurring journal entries submitted from subsidiary ledger systems.
2. Devise computer systems that generate reports of all recurring and non-recurring journal entries and appoint an appropriate level of personnel to review them to ensure proper authorization and supporting documentation exists for each.
3. Appoint an appropriate level of personnel that is knowledgeable with the transaction details to review nonrecurring journal entries as well as a higher level of personnel to approve them.
4. Implement security controls to prevent unauthorized access to general ledger records.
5. Devise appropriate authorization and explanation details that support all consolidation, reclassification, and adjustments of general ledger balances.
6. Program the computer system to restrict journal entry changes outside certain parameters (for example, the system will not allow duplicate account numbers or it will only allow liability accounts to be created with a certain range of account numbers).

B. Journal entries are accurately and completely recorded on a timely basis.

Business risks

- Journal entries will be omitted.
- Journal entries will be posted to wrong accounts and/or in wrong periods.
- Journal entries will not balance.

Control practices

1. Create and maintain one recurring set of period end closing entries/adjustments that includes all necessary entries, including: cut-off, accruals, depreciation, amortization, and valuation adjustments that are necessary for each accounting period-end.
2. Devise accounting systems that automatically generate reports summarizing transactions occurring within subsidiary ledger application systems.
3. Use computer routines to post journal entries to general ledger accounts on a timely basis.
4. Reconcile posted general ledger journal entries to subsidiary ledger records to ensure the entries are complete and accurate.
5. Submit non-standard journal entries on pre-numbered journal vouchers or computer assignment of sequential journal entry numbers approve them before processing.
6. Compare the total amounts posted to the general ledger with predetermined control totals.
7. Devise the computer system to validate journal entries for proper account coding and transaction amount and to report exceptions.
8. Review journal entry detail for use of unusual account codes or high-dollar transactions and investigate and resolve exceptions.
9. Ensure that a one-to-one check of the source documents is completed by the approving manager, including a check of the date to ensure the entry is recorded in the proper period.
10. Ensure that suspended and rejected data as a result of the posting process is isolated, analyzed, and corrected on a monthly basis, as necessary.

C. Journal entries are reliably processed and reported.

Business risks

- Unauthorized changes will be made to programs, causing unauthorized processing results.
- Unauthorized versions of either files and/or programs will be used in processing, resulting in unauthorized or incorrect business transactions.

Control practices

1. Implement controls to maintain the integrity of programs used to process transactions (for example, authorization to modify use programs).
2. Use only current, tested, and authorized versions of computer programs for processing transactions.
3. Ensure that all relevant accounts are locked down during the closing process and only key personnel are responsible for the lock down activation.
4. Program the accounting system to automatically cease processing any entry that does not balance and to display an error message for the individual posting the problem entry.
5. Configure the accounting system to display an error message when someone posts a problem entry.
6. Ensure that the recording, approval, and review of journal entries are performed by different individuals with different levels of seniority.

D. Recorded balances are substantiated.

Business risks

- Unauthorized transactions will remain undetected.
- Errors in processing, summarizing, and recording transactions will remain undetected.
- Transactions will not be recorded.

Control practices

1. Confirm significant balances with third parties.
2. Reconcile general ledger balances regularly to subsidiary ledger balances.
3. Compare journal entry activity reports periodically to supporting documentation.
4. Perform a one-to-one check of the listing of recurring period end closing entries/adjustments to the journal entries actually recorded to validate completeness.
5. Ensure that all nonrecurring period end closing entries/ adjustments entered into the accounting system are compared via a one-to-one check of post-input/update reports to information contained in the source documents to verify the completeness and accuracy of all critical field data.
6. Ensure that all recurring and nonrecurring closing adjustments are approved by the appropriate level of management and compared to source documents to verify the documentation is adequate and sufficient.
7. Compare recorded amounts to predicted amounts or subsequent transactions.
8. Compare recorded balances and activity periodically to outside sources of information.
9. Review substantiation procedures to ensure that they are proper and functioning as designed.

E. Recorded balances are evaluated.

Business risks

- Recorded balances will not reflect realistic evaluations under conditions existing at a particular date.

Control practices

1. Ensure that all balances subject to evaluation are reviewed quarterly to determine any necessary adjustments.
2. Analyze key ratios, trends, and variances periodically to determine required provisions for losses, accounts to be written-off, and additional valuation allowances.
3. Review and approve provisions, write-offs, and additional valuation allowances.
4. Use reliable external sources to help with valuations where appropriate.
5. Review methods and formulas used for realization, accruals, and write-offs periodically for accuracy and current applicability.
6. Review all significant asset accounts at least annually to ensure recorded balances do not exceed net realizable values.

F. All necessary reconciliations are complete and accurate.

Business risks

- Unreconciled discrepancies will exist between the subsidiary ledgers and control accounts, and between related accounts.
- Clerical and/or mechanical errors will occur in the reconciliation process.
- Reconciliations will not be performed on a timely basis.
- Closing procedures will not be consistent across all business units and departments.

Control practices

1. Ensure that all business units and departments use standard reporting formats for reconciliation purposes.
2. Ensure that accounting personnel perform daily or weekly reconciliations of sub-ledger information posted to the general ledger and that management reviews these reconciliations.
3. Ensure that all significant financial statement accounts are reconciled to the general ledger on a monthly basis and that reconciling items are investigated and resolved in a timely manner.
4. Reconcile interrelated balance sheet and income statement accounts.
5. Review reconciliations for mechanical and clerical accuracy.
6. Require management review of reconciliations for reasonableness and completeness.
7. Communicate in writing the deadlines for reconciliations and document key reconciliation procedures.

G. Performance measures used to improve the process are reliable.

Business risks

- Inaccurate performance measures will create erroneous perceptions about process performance, resulting in inappropriate decisions.
- Performance measures will be calculated using inaccurate data and will drive behavior that is inconsistent with management's objectives.

Control practices

1. Collect data to ensure the close-the-books process is performing optimally.
2. Assign employees responsible for the closing process to periodically analyze performance measures to ensure the close-the-books process is performing optimally.
3. Assign management and users of financial information to provide regular feedback about the responsiveness of the closing process to those responsible for closing the books.