

FAST CLOSE

A Guide to Closing the Books Quickly

Steven M. Bragg



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*To Richard Souders,
who always operates at warp speed.*

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Accounting and Finance for Your Small Business

Accounting Best Practices

Accounting for Payroll

Billing and Collections Best Practices

Business Ratios and Formulas

Controller's Guide to Costing

Controller's Guide to Planning and Controlling Operations

Controller's Guide: Roles and Responsibilities for the New Controller

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Cost Accounting

Design and Maintenance of Accounting Manuals

Essentials of Payroll

Fast Close

Financial Analysis

GAAP Implementation Guide

Inventory Accounting

Inventory Best Practices

Just-in-Time Accounting

Managing Explosive Corporate Growth

Outsourcing

Payroll Best Practices

Sales and Operations for Your Small Business

The Controller's Function

The New CFO Financial Leadership Manual

The Ultimate Accountants' Reference

Also:

Advanced Accounting Systems (Institute of Internal Auditors)

Run the Rockies (CMC Press)

Contents

| | | |
|------------------|--|-----------|
| Preface | | xv |
| Chapter 1 | Introduction | 1 |
| | Different Types of Fast Close | 1 |
| | Benefits of the Fast Close | 2 |
| | Legal Issues Impacting the Fast Close | 3 |
| | Steps to Achieve a Fast Close | 4 |
| Chapter 2 | Your Current Closing Process | 9 |
| | Traditional Closing Process: Basic | 9 |
| | Additional Closing Tasks for the Multidivision Company | 14 |
| | Additional Closing Tasks for the Multinational Company | 15 |
| | Additional Closing Tasks for the Public Corporation | 16 |
| | Problems with the Closing Process | 16 |
| Chapter 3 | Conducting a Review of the Closing Process | 23 |
| | Steps in the Process Review | 23 |
| | Payables Process Review | 27 |
| | Billing Process Review | 27 |
| | Inventory Process Review | 30 |
| | Cash Process Review | 30 |
| | Final Closing Process Review | 31 |
| | Total Duration of the Closing Process | 35 |
| Chapter 4 | Alter the Timing of Closing Activities | 37 |
| | Altering the Closing Mindset | 37 |
| | Review and Correct Subledger Transactions | |
| | Throughout the Month | 38 |
| | Complete the Bank Reconciliation Every Day | 38 |
| | Review Uncashed Checks | 39 |
| | Update the Inventory Obsolescence Reserve | 39 |

| | | |
|------------------|--|-----------|
| | Determine the Lower of Cost or Market | 40 |
| | Calculate Overhead Allocation Bases | 40 |
| | Bill Recurring Invoices | 41 |
| | Conduct a Preliminary Comparison of the Shipping Log to Invoices Issued | 41 |
| | Review Preliminary Rebillable Expenses | 42 |
| | Update the Bad Debt Reserve | 42 |
| | Review Preliminary Billable Hours | 43 |
| | Accrue Interest Expense | 43 |
| | Determine Pension Plan Funding | 44 |
| | Determine Flexible Spending Account Funding | 44 |
| | Accrue Unpaid Wages | 45 |
| | Accrue Unused Vacation Time | 45 |
| | Accrue Travel Expenses | 46 |
| | Reconcile Asset and Liability Accounts | 47 |
| | Calculate Depreciation | 47 |
| | Compile Preliminary Commissions | 49 |
| | Review Financial Statements for Errors | 50 |
| | Complete Selected Financial Reports in Advance | 50 |
| | Deferred Closing Activities | 51 |
| Chapter 5 | Revise the Contents of the Financial Statements | 57 |
| | Alter the Mode of Report Delivery | 57 |
| | Standardize Reports | 58 |
| | Eliminate Cost Reporting from the Reporting Package | 59 |
| | Separate Metrics from the Financial Reporting Package | 60 |
| Chapter 6 | Optimize the Use of Journal Entries and Chart of Accounts | 63 |
| | Eliminate Immaterial Journal Entries | 63 |
| | Standardize Journal Entries | 64 |
| | Convert to Recurring Journal Entries | 65 |
| | Centralize Use of Journal Entries | 66 |
| | Use Journal Entries to Accrue Expenses Delaying the Close | 67 |
| | Automate Journal Entry Postings | 68 |
| | Use Accruals Only for External Reporting | 68 |
| | Define Accounts | 68 |

| | | |
|-------------------|---|------------|
| | Standardize the Chart of Accounts | 69 |
| | Automate Eliminations of Intercompany Transactions | 70 |
| Chapter 7 | Standardization and Centralization | 73 |
| | Impact of Standardization on the Closing Process | 73 |
| | Impact of Centralization on a Multilocation Accounting Department | 75 |
| | Impact of Centralization on a Single-Location Accounting Department | 78 |
| | Incorporating Standardization and Centralization into Acquisition Activities | 79 |
| Chapter 8 | Closing the Inventory Function | 83 |
| | Create an Inventory Tracking System | 83 |
| | Implement Cycle Counting | 88 |
| | Reduce the Amount of Inventory | 92 |
| | Properly Record the Lower of Cost or Market Rule | 102 |
| | Reviewing Obsolete Inventory | 103 |
| | Preventing Obsolete Inventory | 105 |
| Chapter 9 | Closing the Billing Function | 111 |
| | Bill Recurring Invoices in the Preceding Month | 111 |
| | Computerize the Shipping Log | 112 |
| | Eliminate Rebillable Expense Processing from the Core Closing Period | 113 |
| | Eliminate Month-End Statements | 114 |
| | Print Invoices Every Day | 115 |
| | Transmit Transactions via Electronic Data Interchange | 116 |
| Chapter 10 | Closing the Payroll Function | 119 |
| | Automatically Calculate Commissions in the Computer System | 119 |
| | Simplify the Commission Structure | 120 |
| | Install Incentive Compensation Management Software | 121 |
| | Post Commission Payments on the Company Intranet | 122 |
| | Avoid Adjusting Preliminary Commission Accrual Calculations | 123 |
| | Use a Computerized Time Clock | 124 |
| | Use a Web-Based Timekeeping System | 125 |

| | | |
|-------------------|--|------------|
| | Automate Vacation Accruals | 126 |
| | Merge Sick Time into Vacation Time | 128 |
| | Cap the Amount of Vacation Time to Be Carried Forward | 128 |
| Chapter 11 | Closing the Payables Function | 131 |
| | Automate the Month-End Cutoff | 131 |
| | Pay Based on Receiving Approval Only | 132 |
| | Automate Three-Way Matching | 135 |
| | Reduce Required Approvals | 136 |
| | Use Negative Assurance for Invoice Approvals | 138 |
| | Use Procurement Cards | 139 |
| | Have Suppliers Include Their Supplier Numbers on Invoices | 145 |
| | Receive Billings Through Electronic Data Interchange | 146 |
| | Request That Suppliers Enter Invoices Through a Web Site | 147 |
| | Audit Expense Reports | 148 |
| | Automate Expense Reporting | 150 |
| | Link Corporate Travel Policies to an Automated Expense Reporting System | 152 |
| | Issue a Standard Account Code List | 153 |
| | Link Supplier Requests to the Accounts Payable Database | 154 |
| | Automate Payments for Repetitive Processing | 156 |
| | Eliminate Manual Checks | 157 |
| | Use a Signature Stamp | 158 |
| | Ignore Supplier Invoices and Pay from Statements | 159 |
| | Issue Standard Adjustment Letters to Suppliers | 160 |
| Chapter 12 | Closing the Cash Processing Function | 163 |
| | Access Bank Account Information on the Internet | 163 |
| | Avoid Delays in Check Posting | 164 |
| | Collect Receivables Through Lockboxes | 165 |
| | Install a Lockbox Truncation System | 167 |
| | Access Online Check Images from a Lockbox | 168 |
| | Consolidate Bank Accounts | 168 |
| Chapter 13 | Impact of Automation on the Closing Process | 171 |
| | Principles of Fast Close Automation | 171 |

| | |
|---|------------|
| Implement Minor Programming Changes on an Ongoing Basis | 172 |
| Automate General Ledger Interfaces | 173 |
| Install a Web-Based Timekeeping System | 174 |
| Install a Workflow Management System | 175 |
| Install Consolidation Software | 177 |
| Install a Data Warehouse | 178 |
| Install an Enterprise Resources Planning System | 179 |
| Chapter 14 Ongoing Improvements in the Closing Process | 183 |
| Ongoing Improvement Process | 183 |
| Improvement Measurements | 186 |
| Appendix A Comprehensive Closing Checklist | 189 |
| Appendix B Fast Close Policies and Procedures | 193 |
| Appendix C Soft Close Checklist | 205 |
| Appendix D Year-End Close Checklist | 209 |
| Index | 213 |

Preface

One of the most common challenges for the controller is to close the month-end books and issue financial statements as fast as possible. The resulting statements are being demanded by corporate management, outside investors, and the Securities and Exchange Commission (SEC) (for public companies) on the shortest possible time lines. However, the closing process has traditionally been a slow one—several surveys reveal that the average company requires about two weeks to close its subsidiary's books, followed by roughly another three weeks to roll up the results into corporate-level financial statements. Companies with more organized closing systems can reduce this process to about two weeks, and those companies with the best closing processes can reduce the entire interval to four days. These results represent a slight improvement in closing times over the past few years, but there is no massive improvement trend. Thus, companies are clearly having a difficult time shortening the closing process.

This book walks the reader through the process of closing the books and creating financial statements faster. Much faster. The author uses the principles outlined in this book to issue financial statements for a multi-division company in one day and has been doing so for years. Some of the key improvement steps discussed in this book are:

- Shift the timing of closing activities out of the core closing period
- Reduce the contents of the financial statements
- Standardize and automate the use of journal entries
- Standardize the chart of accounts
- Centralize accounting functions
- Adopt inventory tracking and cycle counting systems
- Shift rebillable expense invoices out of the core closing period
- Use a web-based timekeeping system for consulting staff
- Streamline the commission calculation process
- Optimize the approval process for accounts payable

- Link supplier invoice accruals to the purchase order database
- Layer consolidation software onto the existing accounting software
- Integrate an ongoing improvement review into the closing process

These bullet points are only a microcosm of the large array of changes recommended in this book. No single change will achieve a massive reduction in the closing interval. Instead, only by gradually working through the changes listed here, in the order presented within the following chapters, can one expect to arrive at a closing interval that may encompass as little as a single day. Enjoy the journey!

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May 2005

FAST CLOSE



Introduction

Achieving a fast close is a process improvement project that requires the full attention of the accounting staff for a long period of time. Before committing to such a project, one should be clear about what type of financial close works best for a company's specific needs, what kinds of benefits will result, and the general steps required to complete the close. This chapter provides answers to these questions.

DIFFERENT TYPES OF FAST CLOSE

Several variations on the fast close concept have appeared, causing some confusion about the nature of each one. The *fast close* is simply an acceleration of the standard closing process, resulting in approximately the same financial reporting package being issued (possibly somewhat stripped down). The focus of this approach is a careful examination of the closing process to strip out wait times, consolidate tasks, eliminate unnecessary functions, add transaction best practices, and selectively apply automation where necessary. It is a task in which an industrial engineer trained in efficiency improvements would feel quite at home.

The *soft close* is less labor intensive than a regular close, because it does not generate as much information. It is designed solely for internal corporate use, so its end product is only those management reports needed to run operations. With this reduced reporting goal in mind, the accounting staff can eliminate the use of overhead allocations. It may also be possible to stop some accruals and ignore the elimination of intercompany transactions, depending on the level of reporting detail desired. The

soft close is most commonly seen in companies that only issue quarterly or annual reports to outside entities, leaving all other months available for the soft close.

The *virtual close* involves the use of a largely automated accounting system, one that can produce required financial information at any time, on demand. This approach is rarely used and only in the largest companies that can afford to install an enterprise resources planning (ERP) system that automatically consolidates and reports financial information. Also, the underlying transactions that feed into the ERP system must be essentially error free, so an accurate virtual close is really the result of a hefty software investment as well as years of continual process improvements. The financial reports resulting from a virtual close tend to be stripped-down versions of reports compliant with generally accepted accounting principles (GAAP), because this approach avoids the need for such manual tasks as overhead allocation, accrual transactions, and the establishment of various reserves.

If achieved, a virtual close can be useful in fast-moving industries where financial results must be monitored frequently in order to make rapid-fire changes to a company's tactical or strategic direction, or at least to identify problem areas for fast management attention.

BENEFITS OF THE FAST CLOSE

There are numerous benefits to achieving a fast close, which vary based on the perspective of the recipient—company management, outside investors, auditors, and the accounting department. These benefits are:

- *Quicker access to financial information.* Company management generally feels that the primary benefit of the fast close is having access to financial information more quickly, allowing it to take rapid steps to improve a company's strategic and tactical position in the marketplace.
- *Marketing tool.* A company's marketing staff can use the rapid issuance of financial information to trumpet the company's openness to the investing public. This does not necessarily mean that the company will issue sterling financial results, only that it will issue results faster. Still, it implies some level of expertise on the part

of the accounting department in processing transactions and compiling them into reports, and so may impart some level of comfort to investors in that regard.

- *More time for financial analysis.* Closing the books fast does not necessarily mean that one must issue financial statements sooner. An alternative is to spend additional time analyzing the preliminary financial statements in order to issue more complete footnotes alongside the financials at a later date.
- *Improved processes.* Because the fast close improvement process requires careful attention to process enhancement, there will inevitably be side-benefit improvements to many accounting processes, leading to heightened efficiency and fewer errors. Within the accounting department, this may be seen as the top benefit of the fast close.
- *Improved control systems.* Internal and external auditors appreciate the enhanced attention to control systems needed to ensure that information is compiled properly and fast.
- *More time, period.* Although some aspects of the fast close simply push activities into the period either before or after the core closing period, some actions are completely eliminated or at least reduced in size. This results in less total time required for the closing process, which can be used by the accounting staff for a variety of other activities.

Consequently, the wide array of fast close benefits results in multiple supporting constituencies—management, investors, auditors, and the accounting department.

LEGAL ISSUES IMPACTING THE FAST CLOSE

The Sarbanes-Oxley Act has made it more difficult to achieve a fast close. The problem is Section 302 of the Act, which requires formal management certification of the accuracy of the financial statements. Specifically, Section 302 requires that the financial statements of publicly held companies do not contain any material untrue statements or material omissions or be considered misleading. Understandably, those signing this certification want to spend more time ensuring that the financial statements are