BOOK OF SECRETS

FOR THE MONTH-END CLOSE

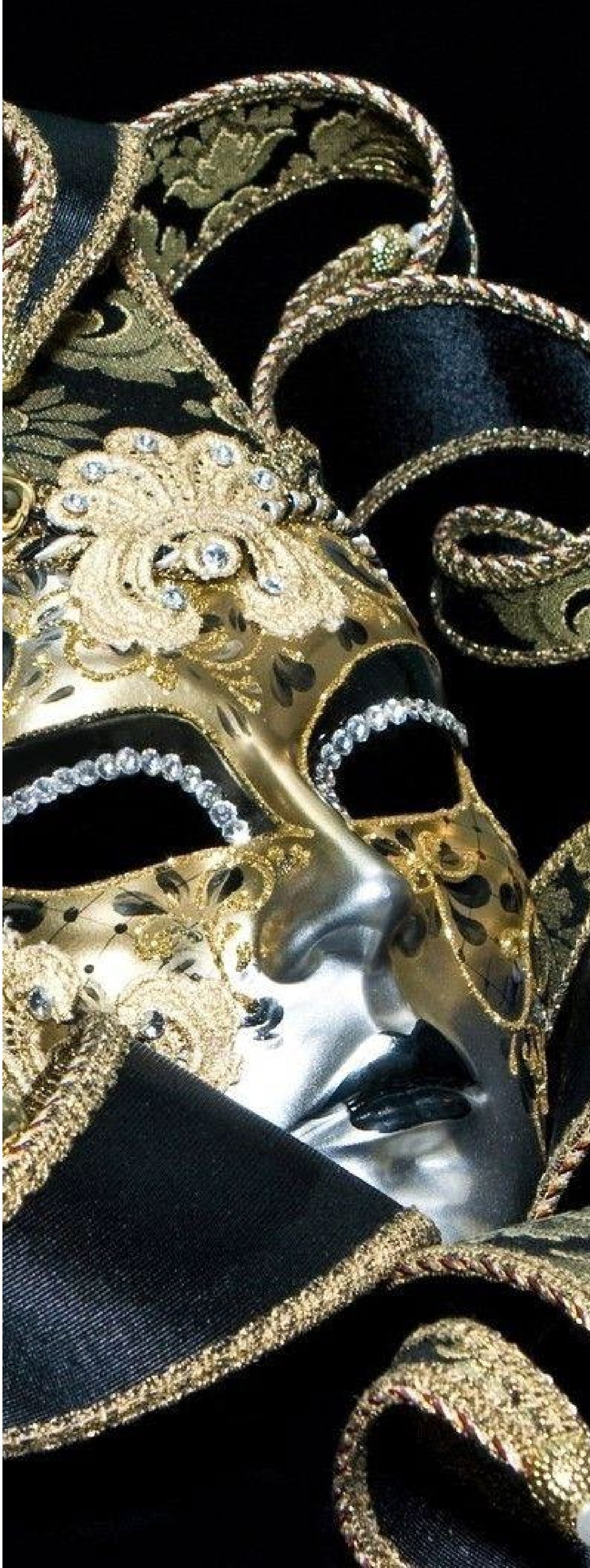
INTRODUCTION

In the post pandemic business landscape, the need to increase efficiency and decrease the cost of day-to-day operations have emerged as a top priority for corporate leaders around the world. Finance and accounting are no exception. CFOs and CAOs from organizations large and small are undertaking transformation initiatives and challenging their team to become faster, leaner and more scalable in the back office. Particularly when it comes to routine and recurring activities such as the month-end close, the demand is at an all-time high.

At SkyStem, we have had the privilege of working with accounting teams from a wide range of industries to help them elevate the month-end close process. What follows are ten open secrets (plus one bonus!) on the month-end close process we want to share with you. These tips are not only simple and actionable, but they can also be easily incorporated into your close process today to take it to the next level.

For more information on streamlining your month-end close, visit us at www.skystem.com

SKYSTEM Crystal Clear Close



Secret #1 – A Good Close Process Starts with the Chart of Accounts

The foundation of the month-end close begins with an organization's chart of accounts. It's the basis of all financial statements. When it comes to the chart of accounts, size does matter. The more active accounts there are:

- The more work will be required at month-end to manage, review, reconcile and flux
- The more work will be required to control access
- The more opportunity for a journal entry error to occur

Each organization needs to determine the correct number of accounts required to run the business, and there is no one-size-fits-all benchmark for what a chart of accounts is supposed to look like. But it is worth reviewing your current setup, because it is very possible that your company's current chart of accounts may need to be right-sized due the following reasons:

- Changes in product and services offerings
- Expansion or contraction in operations
- Acquisitions and divestitures
- Regulatory requirements
- Loosely controlled process for account creation

SECRET #2 – "ALWAYS BE CLOSING"

Taking a cue from the film *Glengarry Glen Ross*, the close process doesn't have to start on Day 0. In general, leading practice guidance suggests that accountants should start as many closing tasks as possible before Day 0. We would go even further to suggest that we perform daily activities with an eye towards the month-end close.

What do we mean by this? For example:

For traditional month-end activities that tend to consume more resources during the close, consider converting those activities into weekly or even daily tasks, as opposed to performing the task once per month. Credit card reconciliations, for example, may benefit from weekly or daily reconciliation if they tend to take an inordinate amount of time during month-end.

Begin investigating open items during the month and resolving them before the end of the period, so these items do not become yet another deadline during the close. This has the added benefit of giving accountants more time to work through issues during the month, as opposed to feeling rushed and having to choose speed over accuracy.

For recurring journal entries, accountants can begin the calculation and journal entry set up during the month, and then finalize them at month-end.

SECRET #3 – MASTER THE ART OF PRECISE ESTIMATES

"Precise estimates" may sound like an oxymoron. In the world of the month-end close, understanding how to use estimates can make a difference between a fast close and one that lags.

When estimating an amount to record after cut-off, the key is to ensure that the calculation process is robust, well-supported and documented. In addition to using true values from past periods for the estimate, the team should also consider:

- Special factors from your vendor or customer that could deviate from past performance
- Internal changes, such as headcount, that could affect the estimate
- How accurate past estimates were compared to actuals

Switching to month-end estimates on even one or two items can sometimes shorten the critical path of the close by a factor of one day or more. Even without the pressure to close faster, accounting teams are encouraged to consider employing precise estimates to deliver performance to management and the field faster.

SECRET #4 – UNLEASH THE POWER OF RECONCILIATIONS

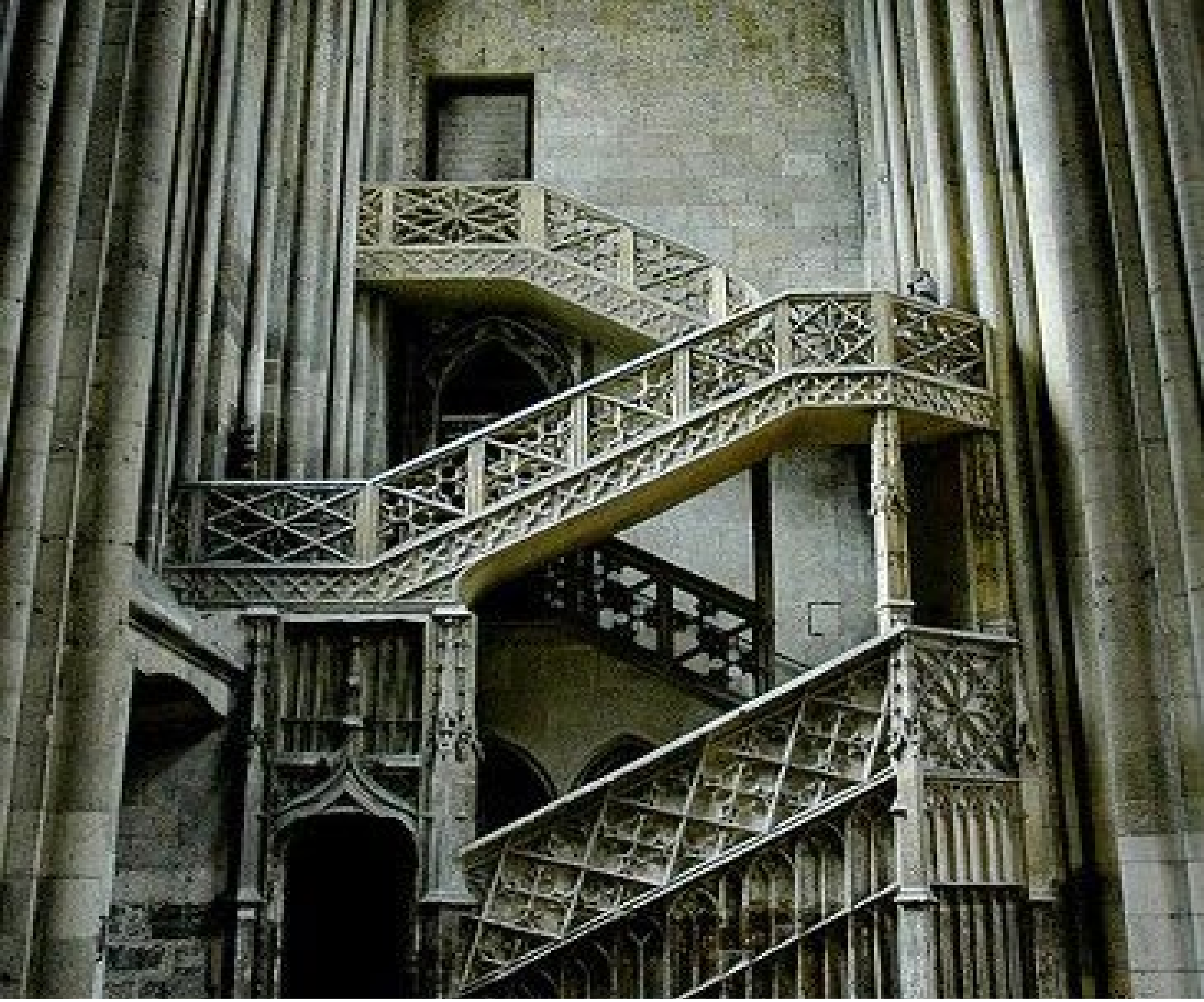
The balance sheet reconciliation is one of the most underrated key controls during the month-end close. Oftentimes it's seen as an administrative activity and a necessary evil. Because of this misconception, it's common to see reconciliations completed in ways that undermine their intended purpose of preventing and detecting errors and fraudulent activity in the financials.

Let's revisit the concept of reconciliations and how to perform them properly.

A balance sheet reconciliation is the comparison of the ledger balance of an account to another source of financial data, such as a Bank Statement, a Subledger or another source. There are three major focus areas regarding balance sheet reconciliations that can affect the health and accuracy of the balance sheet.

Secret #4 – Unleash the Power of Reconciliations

- Reconciliations need to be completed correctly. True reconciliations demand that the preparer reconcile the entire ending general ledger balance. A reconciliation is not a transactional roll forward between the previous and the current period.
- Reconciliations need to be supported properly. All material supporting items must be accompanied by source documents that prove the accuracy and validity of the balance. Source documents would ideally come from outside third parties, such as a bank statement. When that is not available, source documents can be gathered from internal system reports, such as a subledger. If both are not available, the preparer can use an internal calculation, such as a spreadsheet model.
- Timing of the work matters. Reconciling key accounts 20 days after month-end has a different effect than reconciling them 5 days after month-end. The sooner the accounts can be reconciled, the sooner errors and red flags can be caught, investigated and adjusted in the financials. Speed dictates how much reconciliations can contribute to the financial reporting process.
- Handle aged open items and exceptions. Some examples of aged open items and exceptions are: Variances that cannot be reconciled, timing differences aging over 90 days, or proposed journal entry adjustments that don’t get booked. To the extent these items exist on the reconciliation, they need to be tracked, aged and written off after 90 days if they cannot be resolved.



SECRET #5 – USE A CHECKLIST (EVEN IF YOU DON'T THINK YOU NEED ONE)

Due to its simplicity, a checklist is not often taken seriously by finance and accounting professionals. Highly trained professionals sometimes scoff at the idea of following a close checklist because it's hard to believe such a rudimentary tool can help improve performance.

Contrary to common beliefs, the professional checklist was originally created in the airline industry to help manage complicated processes that must be executed by multiple individuals working in synchronicity so that they may achieve a repeatable and successful outcome. The month-end close process is one of the best environments in which a checklist can contribute to a strong and stable close month after month.

Secret #5 – Use a Checklist (Even If You Don't Think You Need One)

What should a team include in their closing checklist? Start with the following and adjust as needed:

- The activity that needs to be done
- The area or department of the activity
- Frequency of the activity
- Risk or priority level of the activity
- Task owner and task reviewer (if applicable)
- High level Instructions to complete the task
- Location of information needed to perform the task
- Special note or reference number (if applicable)
- Due Date
- Current Status
- Completion Date
- Whether the task was completed early/on time/late

Require the team to follow and update the checklist each month as the closing process progresses. This ensures the team is on the same page in terms of completed and incomplete tasks. A checklist also provides information for post-close analysis, which we'll talk about next.

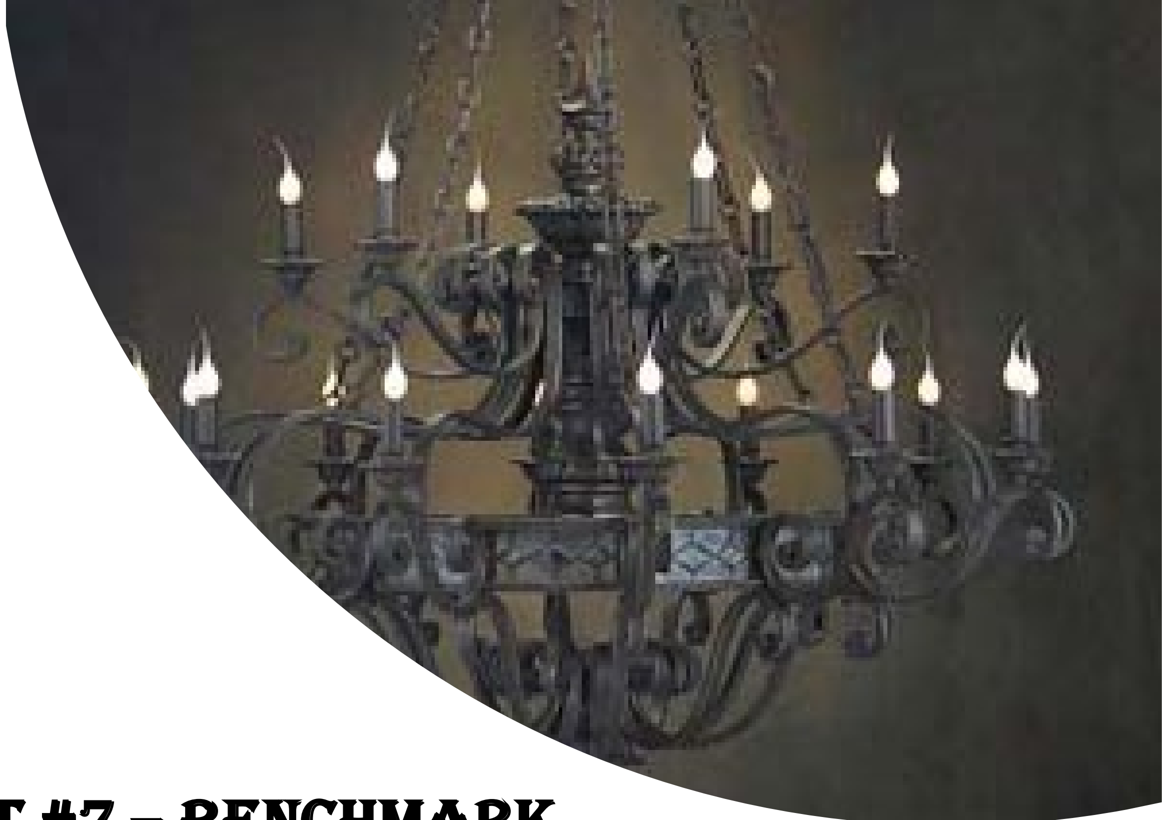
Secret #6 – Build in Elements of Process Improvement

Teams that incorporate elements of process improvement on a recurring basis tend to improve faster, with less resistance to new initiatives. The month-end close is a superb candidate for process improvement because it is a critical part of financial reporting and a recurring process that allows testing of ideas quickly.

Process improvement doesn't have to be a big undertaking. Frequent implementation of small ideas and suggestions can improve the process measurably over time. Nondisruptive process improvement centers on two concepts:

1. Make small improvements. A big idea is disruptive. A big idea requires others to make big changes, which in turn will ignite more resistance and skepticism. A small idea, on the other hand, can be applied gently into the process without commotion. When a big idea fails, it can feel like defeat. When a small idea fails, less is at stake and it's easier to brush ourselves off and try something new.

2. Test quickly. Implement new ideas and assess results quickly. If successful, continue to incorporate into the month-end close process. If unsuccessful, abandon it and move on to the next idea. When small improvements are applied quickly, we protect the mental resources of our team. Instead of wearing out our team by asking for prolonged process changes, we are better off by demanding fast feedback and taking decisive action.



SECRET #7 – BENCHMARK YOUR PROCESS BUT DON'T LET IT RULE YOUR WORLD

Benchmarking against our peers helps us better understand how other teams are deploying their people, process and technological resources. This can inform our own decisions when it comes to how we can refine the month-end close process. There are numerous ways to benchmark, including by industry, by revenue size, by department headcount and by the chosen ERP. Similarly, many metrics are available to measure, including days to sub system close, days to close, number of manual journal entries, cost of the close process, etc.

Do remember that every team is dealt a unique hand. While one team may routinely close in three days, a fast close may not be as feasible for another team. Outside of unique industry conditions and ownership requirements when it comes to financial reporting, several other factors can impact the speed of the close, including:

- Number of people available to assist with the close process
- Competency and skill level of the general accounting department
- Number and quality of tasks completed during close
- Sophistication of the ERP and/or sub systems
- Access to month-end close automation
- Mastery in using estimates

While the use of benchmarking is highly beneficial and should be employed, the ultimate goal of this activity is to provide the accounting team with confidence in making informed decisions to manage available resources effectively.

SECRET #8 – HEIGHTEN FRAUD AWARENESS

Occupational fraud is on the rise. Generally, between 12% to 15% of occupational fraud occurs in the accounting department. Sometimes there are red flags and paper trails that can signal the fraud event in the month-end close process. To catch them, we must heighten our fraud awareness senses.

Look for tampered or fabricated documents – 39% of the time, frauds are concealed through fabrication of physical documents. 32% of the time, they are concealed by altering an authentic physical document. The month-end close process involves reviewing a plethora of documentation before finalizing the financials, so it is critical that accountants remain alert in this area. Below are some tell-tale signs that a document may not be genuine.

ACFE 2022 Report to the Nations

Secret #8 – Heighten Fraud Awareness

- **Typos**: When a standard form contains a misspelled word or a punctuation error, professional skepticism should be elevated. It is uncommon to see typos on official documents such as invoices, letterheads or applications. This could be a sign that the document has been fabricated for the purpose of fooling the approver.
- **Copy and paste jobs**: Faint gray shadows on the edges or certain texts or numbers could be a sign the original content has been doctored and scanned over with new information.
- **Differences in letter font or size**: Sometimes it's difficult to exactly replicate the font or size of an authentic communication. Instead, fraudsters will select the next best font or closest font size when altering the document. This results in different fonts and sizes that are very close, but not exactly the same, as the rest of the document.
- **Documents that look too neat:** Most physical documents under review during month-end close are received in the past and stored until month-end review. In this case, there should be creases, folder marks, potentially evidence of handling and transit and other signs of wear and tear expected. When a document looks too clean, it could mean that the document was fabricated recently and is "fresh off the press," so to speak.

When in doubt, retrieve the source document independently to double verify the authenticity of what is under review.

SECRET #9 – LEVERAGE INTERNAL AUDIT

Internal Audit reports to Management and the Board. Its most visible function is to make sure that your external audit goes well without a hitch. But they have an operational role as well. Beyond helping management establish a sound governance structure, internal audit also has responsibility to help the business become more effective and efficient.

The month-end close is an area where, through a high value operational audit, your internal audit could help take the process to the next level. When we partner with our internal audit team:

- They extend the existing accounting team. Our plates are full. Day-to-day issues tend to consume our normal course of work, and it is very difficult to take time out of packed schedules to work on one-time projects. By inviting internal audit to review our close process from an operational improvement perspective, we are bringing in extra dedicated resources while our team can continue to focus on the day-to-day.
- They establish accountability. Working on "what's not broken but could be better" within month-end close is seldom a first (or even second) priority for management. The involvement of internal audit may raise the priority level and hold management and the accounting team accountable to action items that result from the audit.

When working with internal audit on audit planning, be sure to include the voice of the accounting team. This means:

- Be specific on what the team's objectives are
- Be clear on the scope of the audit
- Communicate any limitations early on
- Agree on a timeline

Secret #10 – Automate, Automate, Automate

Automation is the secret sauce to closing the books faster. It allows more accuracy and control, with less work. When automation is introduced to the close process:

- Spreadsheet usage is reduced by 50% or more
- Reconciliation volume is reduced by 10% to 40%
- Accounting team has access to real-time dashboards to track close progress
- On-demand reports on the close process can be generated and distributed
- Closing checklist(s) regenerate each month automatically
- Email alerts replace the need for manual "check-ins"
- Shared drive usage can be reduced or eliminated
- No more paper!
- Time spent preparing for audits is reduced
- Employee turnover and onboarding process is dramatically streamlined

As companies adapt to a changing business landscape, the need to ruthlessly streamline the month-end close process is increasingly necessary. Manual process improvement tactics have limits in terms of their efficacy. Automating the close process and taking as much work as possible out of the hands of the accounting team is the next step in modernizing the month-end close.

Bonus Secret – Never Stop Learning and Evolving

Every corporation performs a month-end close in one manner or another. This means that learning opportunities are everywhere. Colleagues and peers can be excellent resources in sharing good tips and best practices they may have experienced at their current or previous places of employment. Be open to considering these lessons learned and potentially adapting your own process.

Both paid and free resources on the close process such as e-books, whitepapers and webinars are abundant for those willing to spend some time to develop expertise in this area. Encourage the accounting team to take advantage of these channels and be kept up to date on latest leading practices. Then empower them to take that knowledge back to the team for adoption.

When hiring new talent to join your team, give weight to those exhibiting a change-ready attitude. Finance teams that are resistant to change tend to be the last to modernize, thus losing out on benefits that their more change tolerant peers and competitors experience. This leaves the organizations more burdened with manual work, less likely to access key insights quickly and less competitive in the marketplace.

ABOUT SKYSTEM LLC

Headquartered in the heart of New York City, SkyStem delivers a powerful month-end close solution for organizations seeking to streamline their financial processes.

The company's flagship solution, ART, is an enterprise technology that helps CFOs and Controllers shorten the month-end close and the time to issue financials by automating balance sheet reconciliations, managing month-end tasks, performing flux and variance analysis and providing insightful reporting.

The web-based solution streamlines and eliminates up to 90% of manual activities while strengthening internal controls and corporate governance.

Visit www.skystem.com to learn how you can close faster and win back your time.

SKYSTEM Crystal Clear Close