

# Avoidance of Year-End Deluge by Planned Administration of the Accounting Practice

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*Some highly practical recommendations for promoting internal economies in the management of an accounting practice and for distributing the heavy burden of closing audits throughout the year are offered in this paper, in an effort to minimize the severity of the usual year-end pressure.*

**T**HE severity of the burden imposed by year-end closings is experienced by most accountants. The impact is particularly onerous for small and medium-sized accounting firms that cannot afford to employ temporary help to absorb the additional work.

## Remedial Measures

As with all controversial issues, in this instance as well, there exists a diversity of opinion as to the most practical method of resolving this problem.

One solution advocated by accountants has been that of staggering the closing period of their various accounts. However, not many commercial enterprises will consent to adopt a fiscal year merely for the convenience of their accountants. Furthermore, in the event of the engagement of new accountants by a concern, its fiscal year would have to be changed to conform to the needs of the new auditors. Therefore, this remedy does not appear to be adequate.

With respect to this subject a program has been initiated to persuade

commercial enterprises to establish their natural business year as their fiscal year. This trend should be encouraged since financial statements reflecting the natural year, rather than an arbitrary fiscal or calendar year, would present a more accurate picture of operations for the period covered. However, no substantial benefit will be derived from this innovation by practitioners specializing in one or two industries, since the bulk of their closing audits will still coincide.

As indicated by implication in the introduction, the employment of temporary help affords a second means of alleviating an oppressive tax season. However, this expedient will usually prove to be prohibitive economically. It is manifest that a great deal of time must be devoted to the instruction of such personnel with respect to the requirements of the various clients. By the time these employees have finally obtained the desired productive capacity, their period of employment has expired. Moreover, their rate of compensation generally exceeds that of the regular staff. Consequently, the value of the work performed by temporary employees will not be commensurate with their remuneration.

A third remedial device is that of distributing the year-end peak load throughout the period. Pursuant to this method, preliminary work relating to "closings" should be performed during slack intervals prior to the report date. It is this author's belief that the latter solution is the more desirable approach.

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Before elaborating upon this subject, it would be pertinent at this point to consider the special features characteristic of closing audits. Some of the more time-consuming procedures which distinguish year-end audits from interim examinations are the circularization of confirmation requests, determination of adjusting and accrual entries, writing of reports, review of reports, and the preparation of tax returns.

For purposes of averting year-end congestion, the objectives with respect to the foregoing operations should be twofold. First, wherever possible, the stated procedures should be performed during the financial period. Second, time-saving policies should be implemented with reference to the remainder which can only be effectuated at year-end. In the ensuing paragraphs, each of the foregoing items will be discussed with the intention of indicating some practical means of attaining the desired goal. It is to be noted that the following recommendations apply, primarily, to firms performing continuous audits.

#### **Pre-report Date Confirmation of Accounts Payable and Receivable**

With reference to confirmations, the verification of vendors' accounts and customers' receivables is the most time-consuming. Hence, it is recommended that these items be circularized as of one month prior to the closing date, say November 30th. In connection with the payables, since no balances are usually placed upon related confirmation requests, the forms may be prepared and mailed as early as mid-November. In this manner, all work relating to the confirmation of accounts receivable and payable may be completed in December. Inasmuch as the time required for the independent verification of sundry balance sheet items (e.g., bank balances, etc.) is negligible, such assets and liabilities may be circularized as of the year-end. The utilization of standard forms will limit the typing required therefor. Many firms are inconsistent

in their policy with respect to the responsibility of preparing independent verification requests. Whereas those for payables and receivables are usually typed by the client, confirmation forms for the sundry items are completed by the accounting firm. There is no reason to distinguish between these two groups. The preparation of the latter as well as the former should be delegated to the client.

In the author's opinion, the confirmation of accounts receivable and payable prior to the report date should not nullify the credibility of the accountant's opinion. The usual examination performed during the auditing of December's operations should be sufficient to detect unauthorized transactions occurring subsequent to November 30th. In addition, the inspection of shipping memoranda, payments received subsequent to December 31st, creditors' statements, unfilled purchase orders, and payments made subsequent to December 31st, and the like, would be adequate to substantiate the validity of December's operations.

Hence, the recommendation will contribute to the amelioration of year-end pressure without impairing the integrity of the accountant's certification.

#### **Recording of Accrual Entries by the Client**

The preparation of the report by the accountant is usually preceded by the extraction of a trial balance from general ledger accounts. Upon the completion thereof, it is customary to record all adjusting entries on the worksheet. The final procedure involves the extension of each item either to the profit and loss or balance sheet columns provided for this purpose.

Barring unique circumstances, the prevailing practice does not represent the most expeditious course for the transfer of general ledger figures to related financial statements. As outlined above, the drawing up of the trial balance, the insertion of items in the

proper columns, and the final transcript to the report constitutes a three-fold recording of these figures. Hence, not only is this method unnecessarily time-consuming, but it also provides greater opportunity for the commission of errors. Moreover, the January work of the client is usually impeded due to the inevitable delay by the accountant in submitting the adjusting and closing entries. To remedy the foregoing, it is suggested that the internal accounting staff of the client be instructed with respect to the preparation of the necessary adjusting entries. Most accrual entries such as depreciation, mortgage interest, and the like can be recorded monthly. Only errors would have to be adjusted by the auditor. Under this procedure, the book figures may be transcribed directly to the accountant's report, without the formality of a trial balance worksheet. The tax accruals may be computed by the accountant from the profit and loss statement.

The adoption of this procedure would be of benefit to both the accountant and his client. As indicated previously, the current month's bookkeeping would not be delayed due to the delinquent submission of the adjusting and accrual entries by the auditor. Secondly, the public accountant's time would not be consumed by the preparation of entries which could be determined by the concern audited. Consequently, more time can be devoted to the examination of records.

With reference to the accountant, the elimination of the triplicate repetition of book figures would accelerate the completion of his work. Secondly, the preparation of the accruals by one party and the checking by another would assure greater accuracy.

In this connection, your attention is directed to the practice observed by many principals and supervisors involving the checking of the transcription of accounts from the trial balance to the report. It is manifest that this alleged safeguard will not be available under the proposed system. However,

no practical benefit is derived from this feature of internal supervision since it does not provide any means of detecting errors incorporated in the initial trial balance. Hence, the elimination of this superfluous operation will represent another time-saving aspect of the proposed system.

### **Skeletonization of Reports During the Year**

The most time-consuming feature with regard to the preparation of financial statements is the transcription of the descriptive written matter, exclusive of the monetary figures. Therefore, wherever possible all worksheet copies of reports should be prepared during the year. This can be readily accomplished in those instances where statements do not vary substantially from one period to the next. It is to be noted that the vertical spacing of certain graph paper (6 lines to the inch) corresponds to that of the average typewritten matter (small type). Therefore, the graph paper can be superimposed upon the financial data of an extra typewritten copy, leaving the pro-forma descriptive section exposed. The current year's figures may then be inserted on the graph paper. In this manner, the time devoted to report writing will be negligible.

Those reports that do differ from year to year should also be reproduced prior to the closing audit. As the year-end approaches, the senior in charge of an account should ascertain the modifications to be inserted in the current report. Thus, these variations may readily be incorporated in the pro-forma statements. The benefits derived from skeletonizing statements during the interim are two-fold. First, the year-end work is substantially reduced. Secondly, since the reports will be prepared during slack intervals, rather than under tax-season pressures, more time can be devoted to composition and form, thereby assuring a satisfactory presentation.

### Standardization of Audit Work Papers to Facilitate Review of Reports

The importance of standardized and indexed workpapers has been underestimated by many firms. Consequently, the review of reports by principals, prior to submission for typing, usually necessitates the presence of the senior who is familiar with the audit papers. Furthermore, since the workpapers have not been compiled uniformly, even the senior will experience difficulty in locating material contained therein. This writer can testify from past experience, that where workpapers are arranged haphazardly, as much time can be spent in searching for supporting schedules and data as in the actual checking of the reports. Such a situation is definitely not desirable, especially when time is of the essence.

To rectify this condition, workpapers should be standardized, indexed, and cross-referenced. A simple method of maintaining adequate papers is presented for your consideration.

Instead of the "orthodox" vertical folder utilized by the average practitioner, it is suggested that workpapers be filed in a loose-leaf three ring binder. A separate section should be provided for each group of workpapers. For instance, the audit program, monthly trial balances, bank reconciliations, audit notes, petty cash counts, etc., would constitute different divisions. An indexed tab should precede each category. All worksheets should be numbered consecutively and be identified by a symbol or letter disclosing the nature of the workpaper. The audit program should be employed as a table of contents. That is, each man, when initialing the program to indicate the work completed, should insert the page number of the worksheet containing the related schedule.

Generally, the standard 11" x 8½" loose-leaf binder will be the most appropriate for the purpose. It is suggested that eight-column paper, ruled on both sides, be utilized for worksheets. By

the insertion of "short" sheets, it will be unnecessary to resort to the larger size columnar paper. The application of this device will permit the continuation of monthly trial balances, bank reconciliations, petty cash counts, etc., on the same series of worksheets. At the termination of the financial period, the contents of the binder should be transferred to inexpensive manila folders for permanent filing. Thus, the number of loose-leaf covers required will be restricted to a minimum.

As mentioned previously, the trial balance operation will be by-passed and, in lieu thereof, the general ledger figures will be transcribed directly to the report. In order to facilitate the review of financial statements by supervisors, the page number assigned to the respective supporting audit work paper should be placed next to the related item appearing in the report. The notations should be indicated in colored pencil and circled to avoid confusion on the part of the typists.

Numerous benefits may be derived from the institution of the foregoing recommendation. In consequence of the loose-leaf feature, individual pages may be extracted without disturbing the sequence of the remainder, whereas, in the conventional metal fastener folder, all workpapers superimposed over the desired sheet must be removed in the process. The sectionalization of the binder, as outlined above, will facilitate reference to the contents therein. The availability for use of the reverse, as well as the front side of the proposed loose-leaf analysis sheets should substantially reduce the customary size of audit work papers. Furthermore, the extension of monthly data, for bank reconciliations, petty cash counts, and the like, in successive columns on one sheet, rather than employing separate workpapers for each month, should also contribute to the decrease in the number of worksheets required. It is to be noted that loose-leaf binders used currently may be systematically arranged on open book shelves, rather than in

file cabinets. Hence, the inconveniences usually experienced when inserting or removing folders maintained in file cabinets will be avoided.

In summation, the maintenance of uniform workpapers in loose-leaf covers will expedite the location of the pertinent binder and the material contained therein. Consequently, the audit, as well as the review of reports will be accelerated accordingly.

### **Compilation of Data for Tax Returns Prior to Year-End**

As indicated at the outset, the preparation of tax returns constitutes another primary factor contributing to the year-end dilemma. Fortunately, most major tax problems do not arise immediately subsequent to December 31st. They are usually inherent throughout the operating period. Therefore, the time for researching tax questions should be during the year rather than after its termination. Once all crucial queries have been resolved, the completion of the tax forms is a matter of routine. However, even routine can be burdensome if it is permitted to accumulate. Hence, the work relating to tax returns should also be allocated throughout the year.

This distribution may be accomplished in the following manner:

1—Schedules of security transactions should be recorded periodically as they arise.

2—Schedules of depreciation can be prepared during the year. Only the current year's figures need be inserted at the end of the year.

It is to be noted that the tabulations mentioned in items #1 and #2 should be attached to the related tax returns rather than be transcribed thereon.

3—The majority of business expenses appearing on both the federal and state returns are generally included under the heading "other expenses". The recording of these items individually on both governmental forms represent a duplication of work. A substan-

tial savings in time may be achieved by preparing a "skeletonized" listing of the respective items during an idle period. The figures can then be inserted as soon as they are determined. Typed copies of this schedule can be attached to both the federal and state forms.

4—The federal blanks are usually available in the early part of December. A great deal of information can be entered on these forms without waiting until the related reports are prepared. For instance, with respect to form 1120, the federal corporation return, the following information may be entered immediately:

- a. The name, address, etc., required on page 1.
- b. Data concerning the compensation of officers requested under Schedule F, page 2.
- c. The answers to the questions appearing on the bottom of page 3.
- d. The balance sheet at the beginning of the taxable year on page 4, Schedule L.

As enumerated below, the foregoing concept may likewise be applied to the personal tax returns prepared by accounting firms.

1. The compilation of security transactions should be accumulated throughout the year.

2. Where it is customary to prepare the tax return from an examination of the checkbooks and other data submitted by the individual, the analysis thereof should be performed periodically to reduce the year-end work.

3. Usually such tax clients are close acquaintances of the principals of the accounting firm. Hence, this relationship may facilitate arrangements whereby the final data for the year can be submitted during the last week of the year or immediately subsequent thereto. In this manner such returns can be completed while awaiting the closing date of the regular accounts.

4. To avoid duplicating the listing of numerous contributions and medical

expenses for federal and state returns, these items should be recorded on separate schedules. Typed copies thereof may be attached to the respective returns.

5. Special forms (containing the pertinent tax queries) should be provided for clients who are required to supply all related information personally. This will furnish an automatic check list for such clients and will also avoid delay occasioned by the omission of necessary items. In addition, it constitutes a more efficient manner of securing such data.

The implementation of the foregoing recommendations would permit the preparation of a considerable portion of the tax work currently, thereby alleviating customary year-end accumulation.

#### **Streamlining of the Clients' Accounting Procedures**

Normally, many concerns do not close their books until about the twentieth of the month subsequent to the end of their taxable year. Therefore, the intervening period is not available to the average accounting firm for commencement of the closing audits. Since time is of the essence, it would seem advisable to devise some means of accelerating the readiness date of one's clients.

In furtherance of the stated objective, it is suggested that the customary organization of the general ledger be revised so as to exclude the income and expense accounts, if voluminous. In lieu thereof, income and expense control accounts should be established in the general ledger which should be supported by a subsidiary ledger of the related detail.

Under the prevailing practice all income and expense items are usually contained in the general ledger. Moreover, separate ledger sheets are generally assigned to each account. This feature impedes the posting operation in consequence of the numerous pages referred to during the process. In this

connection, you will note that it is the time of a skilled general ledger bookkeeper or comptroller which is consumed thereby, rather than that of a clerk. Moreover, additional labor must be expended to trace errors normally committed in the initial preparation of a trial balance. These substantial disadvantages will be eliminated under the proposed method. As mentioned previously, the detailed expense and income accounts will be transferred to a subsidiary ledger. The arrangement of this register should be in "railroad" columnar form, so as to provide at least 10 to 15 columns to the page. The columnar sequence of the accounts appearing therein should conform to that of the related book of original entry. The posting of the details should be performed by the custodian of the original journal book, say, the voucher register clerk. The general ledger bookkeeper need only enter the aggregate expense figure in the proper control account. This division of labor will reduce the burden of mechanical tasks imposed by the present system upon the skilled employee. Furthermore, the creation of control accounts will facilitate the detection of trial balance discrepancies relating to the detail. The simplification of general ledger routine, as outlined above, should substantially diminish the time required to complete the records.

Another major factor obstructing a timely "closing" by the client is the common practice of delaying the balancing of the voucher register pending the receipt of all anticipated invoices. In view thereof, it is suggested that arrangements be made with vendors to submit all statements not later than the fifth of the month. The books can then be closed as of that date. Any delinquent invoices received subsequently may be recorded by the bookkeeping staff via the general journal.

The implementation of the foregoing should afford the accountant an additional ten to fifteen days within which to complete his work during the tax season, when time is so important.

### **Staff Rotation to Reduce Personnel Turnover During the Tax Period**

It has been the custom of accounting firms to assign men permanently to related accounts. Consequently, the training of juniors and semi-seniors so assigned is limited. The opportunity for learning new auditing procedures would normally be exhausted within about a year. Since such men are interested primarily in acquiring a diversified background, they must ultimately seek new employment as soon as they attain the point of saturation in any one position. The foregoing cycle is principally responsible for excessive personnel turnover. Unfortunately, the time usually selected to effect a change of employment is the tax season. Hence, those accounting firms subject to frequent staff replacements would be deprived of experienced men during the most critical period.

To remedy the foregoing situation, it is recommended that the policy of personnel rotation be adopted. The advantages to be derived from such a practice are as follows:

1. The resulting diversification of experience afforded to staff members would eliminate a primary cause of terminations.
2. The extension of the average term of employment would permit accounting firms to benefit from the products of their training programs.

3. Reduction of personnel changes during the year-end would—
  - a—relieve supervisors of the onerous task of continually interviewing applicants.
  - b—increase the available manpower and hence, the productive capacity of the staff.

In order not to antagonize clients, newly rotated personnel assigned to the various accounts should accompany the present auditors during interim visits. In this manner, bookkeeping staffs will not be continually annoyed with the usual queries made by an accountant on his initial visit. Any loss of time due to the instruction of rotated personnel would be more than offset by the time saved as a result of reduced staff turnovers.

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The adoption of the recommendations contained in the preceding comments should promote internal economies in the accounting firm as well as distribute the major burden of closing audits throughout the year. In addition, the present effective commencement date of the tax season would be about November 15th rather than January 15th.

In conclusion, the cumulative effect of the foregoing should be adequate to overcome the different problems brought on by the accountant's nemesis, the tax season.

