DOCUMENT CONTROL INFORMATION

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| Sub-Process Owner(s) | Martin J Hayter (Finance Manager) |
| Location | Zurich, Switzerland |

Note: Major changes to the process narrative documentation must be approved by the Global Accounting Manager.

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# **Abbreviations & Definitions**

|  |  |
| --- | --- |
| CFO | Chief Financial Officer |
| CR | Credit |
| DR | Debit |
| GL | General Ledger |
| JE | Journal Entry |

# **Policies, procedures & Related Documents**

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| --- | --- |
| **Procedures** | **Description** |
| SE-003 | **Managing Journal Entries Policy**  To provide guidance on the requirements for journal entries, including the need for appropriate documentation and support and what constitutes properly prepared, reviewed, approved and posted journal entries. |
| SE-005 | **Account Reconciliation and Analysis Policy**  To define standards and procedures for balance sheet account reconciliations and analysis. |
| SE-009 | **Global Accounting Policy for Prepayments**  To define the uniform accounting policy for recording prepayments. |

# **Prepayments Accounts & GL Coding**

| **GL Account #** | **GL Account Name** |
| --- | --- |
| 1910000 | Prepayments |
| 7702128 | Amortization Deferred Charges |

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# **Key Personnel**

| **Unit/Department** | **Function** |
| --- | --- |
| Accounting | Finance Manager  Intermediate Accountant  Senior Accountant |
| Property | Property Manager |
| Purchasing | Purchasing Manager  Purchasing Clerk |

# **IT Overview**

The company uses SAP as their enterprise resource planning software, which integrates a number of information systems including the general ledger system, accounts payable module and cash disbursements module. Amortization of prepayments occurs manually in a controlled spreadsheet maintained by the accounting department.

# **Prepayments**

## ***Overview***

As part of its daily operations, Summit Equipment utilizes plant and machinery equipment to produce its products. Each piece of equipment are individually insured by multiple policies written by third-parties to cover potential loss exposure due to damage caused by business interruptions (these interruptions are specifically defined as part of the insurance policies). The Company’s fiscal year is on a calendar year end. The Company holds various insurance policies that were entered into when new equipment was purchased. In accordance with **SE-009 Global Accounting Policy for Prepayments**, the Company defers the insurance premium amounts when paid and amortizes it over the life of the respective policy (all policies are twelve months). All policies are renewable annually.

# **Prepayments Process Narrative**

## ***Obtaining New Property Insurance***

Upon purchase of new equipment, the property manager prepares and sends an e-mail request to the purchasing department to obtain insurance for the newly-acquired equipment. The purchasing department then sends out the details to contracted insurance companies and asks for price quotes. The property manager reviews each draft insurance policy for appropriateness of coverage and then approved by the purchasing manager. The draft insurance policies are forwarded to the accounting department for recording into the spreadsheet and also for preparation of disbursement request.

**Note- this process is out of scope for purposes of testing within the amortization of the prepayment account.**

## ***Recording of Prepayments***

The intermediate accountant reviews the documents and prepares an accounts payable voucher based on the amount in the payment request form. He/she reviews the terms of the insurance policy and determines if it will meet the global accounting policy for recording of prepaid expense. If the item meets the policy, the following journal entry is drafted:

DR – Prepayments

CR – Payables – Domestic suppliers

If the transaction does not meet the criteria, the intermediate accountant posts the following journal entry:

DR – Insurance

CR – Payables – Domestic suppliers

The senior accountant obtains a copy of the insurance policy and reviews the terms and conditions, including the amount of insurance premiums to be paid. He/she then determines, based on the details of the contract and the Company’s accounting policy for prepayments, whether the transaction should be recorded as a prepayment.

The senior accountant matches the details in the draft JE, such as the amount of insurance paid, date, and description, to the AP voucher and insurance policy. He/she then makes an independent assessment on whether the transaction qualifies as a prepayment based on the accounting policy (compares the accounting policy to the terms of the insurance policy). If an exception is noted, the senior accountant returns the draft JE and AP voucher to the intermediate accountant with specific instructions on what to change. The intermediate accountant revises the entry or amount in the JE and/or AP voucher and forwards it to the senior accountant for review. The review process repeats until all exceptions are addressed. The senior accountant documents the review by placing a tick mark on the AP voucher and insurance policy as evidence of the tie out procedure and approves the transaction by affixing his/her initials in the AP voucher and posting the entry into the system (**control #1**).

The documents will be forwarded to the treasury department for payment scheduling and recording into the payable system/ledger. Once the amount has been entered into the system as to be paid, it follows the purchases process as included within the **Purchases Process** narrative.

When the intermediate accountant concludes that an invoice is a prepayment, it is added within the prepayments monitoring spreadsheet. The intermediate accountant updates the spreadsheet monthly and includes the insurance premium amount, term, and respective amortization period. The amortization is automatically calculated within the spreadsheet based on terms and the current month.

# **Prepayments Reporting**

## ***Monthly Amortization and Disclosures***

Each month, the intermediate accountant prepares a JE based on the total amount of amortization expense for the month in the prepayments monitoring spreadsheet. The pro-forma JE to record amortization expense is as follows:

DR – Amortization Deferred Charges

CR – Prepayments

The senior accountant reviews the prepayments monitoring spreadsheet on a monthly basis. As part of his validation- he separately pulls the summary of new insurance policies entered into for the current month and checks to determine that they were properly recorded and included on the spreadsheet. He/she checks the clerical accuracy of the schedule by recomputing the amounts in the spreadsheet. He/she then matches the amount in the JE to the total amortization per month as is calculated within the spreadsheet. If there are any exceptions, the senior accountant sends back the JE to the intermediate accountant with specific comments based on the review. The intermediate accountant prepares a reconciliation explaining the difference and adjusts the spreadsheet based on the reconciliation made (if necessary). The review process repeats until all exceptions are addressed. The senior accountant documents their review by placing a tick mark on the monthly total column of the spreadsheet as evidence of the tie-out procedure and signifies his/her approval by posting the JE into the system(**control #2**).

The Finance Manager reviews the information contained in the prepayments monitoring spreadsheet on a monthly basis, such as the insurance premiums paid, terms and amortization period, against the JEs posted in the system and compares the information to source documents as applicable. The Finance Manager then compares the amounts of prepayments and amortization expense against the monthly budget. The senior accountant prepares a reconciliation and explanation of the difference between the budget and actual amounts. When the Finance Manager identifies an unrecorded transaction (i.e., a transaction in the spreadsheet that was not recorded in the system), the Intermediate Accountant prepares an adjusting JE to record the unrecorded transaction and follows the guidance in Section 7.2 of this narrative.

## ***Financial Statement Reporting***

The accounting policy for prepayments is disclosed in the policy footnote in the financial statements that will is reviewed monthly the CFO. This control is covered in the Financial Statement Close Process narrative.

# **Segregation of Duties**

The below describes observations as to any potential conflicting duties.

Incompatible duties may indicate other weaknesses in procedures and controls over authorization of transactions, safeguarding of assets, or asset accountability duties.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Segregation of Duties Table for Prepayments** | **Who performs**  **Procedure?** | **Who records procedure?** | **Who reviews results?** | **Who approves?** |
| Obtaining equipment insurance | Property Manager | None | Purchasing Manager | Purchasing Manager |
| Recording of prepayments | Intermediate Accountant | Senior Accountant | Finance Manager | Finance Manager |
| Monthly amortization and disclosures | Intermediate Accountant | Intermediate Accountant | Finance Manager | CFO |