UNIT 1 OVERVIEW OF RECORD TO REPORT PROCESS

Structure

1.0 OBJECTIVES

After studying this unit, learner should be able to:

- explain the meaning of Record to report;
- discuss the relevance of Record to Report in Organisations;
- describe the importance of Recording and Reporting functions in Business and;
- discuss the reasons for Outsourcing R2R

1.1 INTRODUCTION

Record to Report (R2R) is a term which is very specific to the outsourcing industry for Finance and Accounting (F&A). R2R stands for **Record to Report**.

When we look at any organisation which is writing its books of accounts, it would be recording all the financial transactions in its day books which would be followed by posting them in the respective ledgers and making the Trial Balance. This entire process is about recording. Once the trial balance is done, it is followed by the Profit and Loss and the Balance sheet and it would present these numbers to its stakeholders such as share holders, bankers, financial institution, suppliers, customers and even internal users such as the managemant and employees. These numbers express the health of the company. This is called Reporting.

In this Unit, we intend to have an overview of Record to Report process and discuss its relevance in the business, importance to business and technology which facilitates in this process. We shall also discuss the reasons for outsourcing R2R process.

1.2 RELEVENCE OF RECORD TO REPORT (R2R) AS A PROCESS

Now having seen the various types of entries that are done in the process of recording any transaction, let us also look at the organisations and conditions which impact these transations. The normal journey of an accountant, as we all know starts from voucher and culminates with the final books of accounts, As you have read in the earlier blocks, these could be in any kind of or organisation be it a partnership concern or a privately or publicly held concern.

However, in the global world of outsourcing, we see that big organisation have many units. These units may represent countries, locations, businesses, segments etc. They mostly are separate legal entities over multiple layers of ownership (which are added to the group through merge and acqusisitions). They are part of the same global group.

These large global groups are spread across the globe such as Accenture (the large Information technology giant) or Pfizer (the pharmaceutical giants) or General Motors (manufacturer of cars) or General Electrics etc. Such multinational groups work with thousands of people with different cultures. Their annual sales turnover is in billions of dollars. They raise money in different stock market. As a part of their growth strategy, they normally acquire many companies, which then become part of their groups.

All these large groups have smaller companies within them. These companies operate as individual entities and consolidate with the group. They are responsible for their own P&L. They have their own Fixed Assets (such as assets held for the purpose of producing or providing goods/services, for example Land & Building or Plant and Machinery/Office Equipment) and their own markets where their own or their other group concern produce is sold.

Some of the problems that the parent group would face when they have to consolidate their final group accounts are as follows:

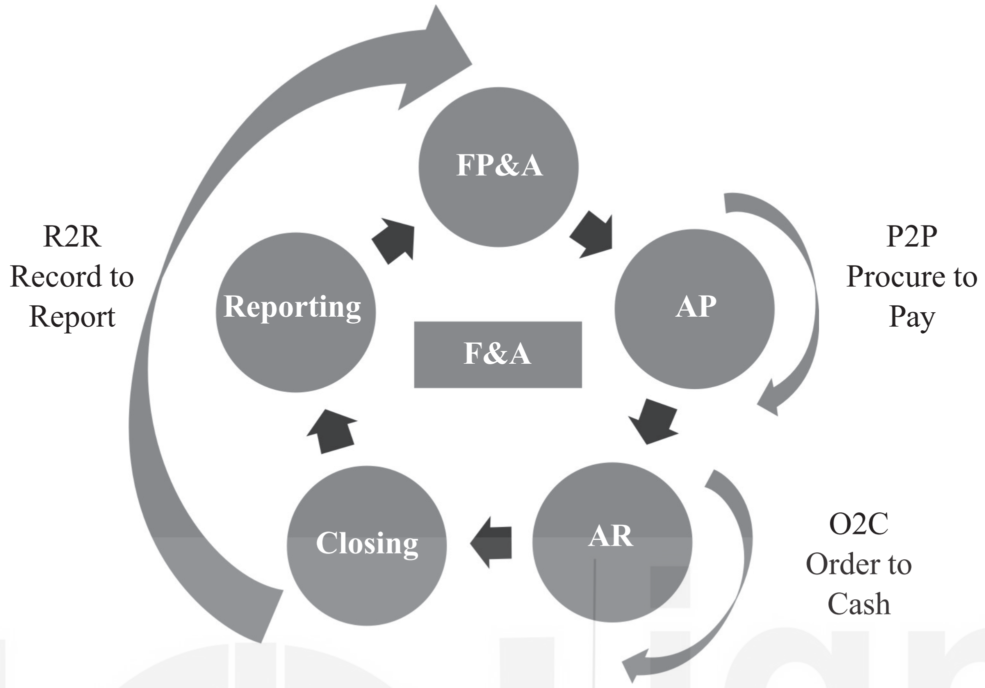
a) units could be closing their books of accounts in different currencies

b) units could be closing their books of accounts in different financial calendars

c) units would be transacting between themselves

d) units would be sharing assets and other resources like Fixed Assets shared among themselves.

R2R also called as A2R (Accounting to Reporting). It includes all the processes from the time we record the financial transactions by way of JE (Journal Entry) or by feeds coming from SL (Sub Ledger) or Sub Systems into GL (General Ledger) till the time financials are reported to both internal & external stakeholder and perform the analysis with actual operating results with the planned numbers. Below is the exhibit of F&A Cycle:



Finance & Accounting Cycle

Therefore it becomes very important to capture the transactions properly and report them. In order to capture these transactions properly there is a need to have standard processes across different units of the large company. The entire business cycle of these large companies is therefore categorized into processes. All the activities from procuring raw materials to paying the suppliers for raw materials are included in one process namely 'Procure to Pay" which is also called "P2P" process. Similarly all the activities from recording to reporting of transactions are included in "Record to Report" or "R2R" process and all the activities from Order (receipt of sales order) to Cash (cash collection and application against customer invoice) are included in "Order to Cash" (O2C) process.

1.3 LIST OF SUB PROCESSES IN R2R

List of sub processes in Record to Report

The Record to report process comprises many sub processes which could be listed as follows:

1. Transaction Processing
2. Intercompany Accounting
3. Fixed Asset Accounting
4. Reconciliation
5. Cash and Bank Management
6. Period close and consolidation
7. Financial Reporting

As we examine the above list, we see that the scope of R2R is very wide and covers almost all the aspects of accounting for any Organisation. R2R is also very core and critical to any business enterprise. Unlike P2P and O2C, R2R is quite high in the Finance and Accounting (F&A) value chain. Outsourcing it is like handing over the entire finance department to an external organisation. This is one of the reasons why R2R is not easily outsourced by global organisations. It is outsourced after a lot of deliberation and after gaining enough confidence in the capabilities and expertise of the vendor team.

As this is not a single process but a series of processes. It is a little difficult to define a set of steps of this process. Having said that, this unit would attempt to define the steps involved in each of the above mentioned processes in the overall R2R process.

1.3.1 Activities in Transaction Processing

Before we define the steps involved in each of the above mentioned processes in the overall R2R process, let us try and understand Chart of Accounts and how the accounting cycle works in any large organisations.

Chart of Accounts:

By Chart of Accounts, we mean the accounting string which is used to book an entry in the accounting software. For example, if we were to book an entry for paying to creditors, simplistic accounting entry would be debit the creditor and credit the cash account.

For a global company there are much more aspects attached to it for booking this simple entry, for e.g., which legal is it, which cost center will it hit, which affiliate is it in respect to, which account digit it will use etc.

There are some common fields in chart of accounts, which in Oracle/SAP parlance would be called as Accounting Flex Fields: **• Legal Entity • Cost Center • Analysis Code • Business Unit • Account • Others**

Legal Entity

There can be many incorporation (Inc. Plc. Ltd etc.) in, which the company operates and must submit their results to the regulatory authorities, e.g. SEC (Securities & Exchange Commission). These legal entities cut across the geographies and are operated in different regions.

Cost Center

These are sub units more from the perspective of FP&A to measure the cost incurred in various divisions like Quality, HR, Finance, Administration etc. This is where the concept of cost center comes into picture to record the cost and revenue at this department level.

Analysis Code

This is the code used to represent the other side of the legal. For e.g. if we are to book an entry between two legal entities within the same organization, we will say A Inc. has lent money to B Inc. In this case, we will show receivables for legal A w.r.t legal B (analysis code) and payables in legal B w.r.t to legal A (analysis code). This codification helps in tacking any disconnects specially in the inter-company accounts. It can also be used as an identifier for deal, type of loan, lease etc.

Business Unit

This is the sub-classification done when one legal wants to segregate the units into different variations, may be based on operations (core and acquisition), regions (NEWS), products etc.

Account

This is the level at which the organization wants to track the figures. All companies define a charter/series, that consist of which account to be used for varied Balance Sheet (BS) and Profit & Loss (P&L) categories.

Others

Any other segment, which the organization wants to track. For example, the VAT code for VAT returns, Loan Code for tracking which agreements exist for the legal being accrued and charged.

In SAP, COA (Chart of Accounts) is a list of general ledgers. It is created at the client level and assigned to each company code. Account group is created in each chart of account with a number range.

There are mainly three types of chart of accounts-

1. Operating chart of accounts
2. Group Chart of Accounts
3. Country-specific chart of accounts.

Large organisations, which have their presence in many countries and operate in multi lines of businesses, have a strong need for executing the entire Record to Report.

Now let us look at how it works:

- Each unit has an onshore controllership team which is responsible for this function.
- The controllership teams send authorised requests for accounting entries into the financial ledgers. They could also send authorised requests for updating the General Ledger (GL) and generate the system reports. These requests are like inputs that go into the overall financial system. Once these requests are given, the process starts and the transaction processing of the financial entries is done. This is followed by the preparation of Financial Reports and their review.
- These entries are then uploaded in ledgers and the requisite reports are generated.
- These are then used by the various controllers to evaluate their performances.

This is a way a Financial Controller would get the R2R cycle completed for his process.

Please note that this cycle can be performed onshore where the controllership team sits or it could be off shore in a far away land that is linked electronically with the controllership team.

The R2R process is carried out in three stages as defined below:

1. The Setting Up Stage
2. The Execution Stage
3. The Communication and Control Stage.

Let us look at all these stages individually.

1. <u>The Setting Up Stage</u>

The setting up stage is when the controllership of the organisation would be setting up the rules and regulations for being able to effectively conduct the record to report function .The policies and procedures for executing Journal entries are established and communicated by the organization to the operations teams. Besides, all the necessary formats and templates are also established and communicated.

The operations teams are trained to understand the policies, procedures and templates so that they are executed and maintained in the intended way. Another very important aspect of record to report is the technology that we have to decide at the time of setting up. Should it be a standalone financial accounting package or should be complete integrated ERP systems. It could also be a client server or completely web based one, depending on where are the locations of units etc.

2. <u>The Execution Stage</u>

Once the systems and procedures are set up, the actual execution commences. In the execution process, we have the following steps:

Step 1: The journal entry is created and submitted for review and approval

Step 2: The journal entry is reviewed and approved or is not approved.

Step 3: These journals are then further verified.

Step 4: Journal entries are then posted either through the manual or automated system.

Please note that the examples of a JOURNAL ENTRY include:

a) Adjusting Journal for reconciliation items

b) Accruals for unprocessed invoices & Business expenses & other liabilities

c) Prepayment

d) Payroll (salary Debit, salary payables credit)

e) Fixed Assets (Depreciation debit, fixed assets credit)

f) Inventory

g) Travel & Expense (ref. Procure to Pay)

h) Procurement cards

i) Tax

Types of entries

There are various types of entries that are used to record transactions. These are as follows: -

- Standard or Ad-hoc Requests
- Recurring or Non Recurring
- Auto Reversal or Manual Reversal
- High or Medium Critical
- Profit & Loss and/or Balance Sheet impact
- Usual or Extraordinary

The distinction depends on the perspective of the transaction and how it is to be recorded. On the floor in any F&A BPO, you may hear these terms many a times. So let us acquaint you with some of these terms better.

Standard or Ad-hoc Requests

Standard Entries are those entries that record every month although the amounts vary. For examples these could be (a) Month end provisions (b) Cost Charge-outs or (c) Revenue Share

Ad-hoc Requests are those requests which are not received every month. The reasons for these requests could be as follows:

- These transactions do not take place every month
- Usually processed through the automated ERP system. However they may need to be passed manually due to system failure.
- Entries normally passed by customers but due to certain reasons (leaves/ attrition) the offshore team needs to pass them.

Recurring or Non Recurring

Recurring are those entries that require to be passed repeatedly after every certain period. This may be the case when the amount to be paid each month is the same. E.g. Rent Income or Royalty expense as per the agreement

Non-Recurring is opposite of the above. These entries are not repeatable or do not follow an established frequency. E.g. Maintenance Expenses which could vary based on unknown break downs etc.

Automated or Manual Entries

Automated Entries are those entries which are generated by the system directly.

Manual Entries are the entries which are done manually. For e.g. any entry uploaded by the journal entry system into the mainframe system is a manual entry (as the entry needs to be uploaded manually) or preparation of an excel sheet.

Auto Reversal or Manual Reversal

Before we understand the nature of these entries, we have to understand the rationale behind why do we reverse any entry. Reversing entries are a useful tool while dealing with accruals and deferrals. Their use is optional and depends on the accounting practice of an organisation. A Company may choose to reverse an entry to reduce the chances of error in allocating a transaction between two accounting periods. For instance: We were expecting a bill from the services Vendor for May. However, he could not provide it on time so we made provision for outstanding expenses at the end of the month May.

The entry made is: Expense Dr (booked in the profit and loss account); outstanding expense Cr (liability in the balance sheet). This accrual would to be reversed in June (Outstanding expense Dr. Expense Cr). When the bill is received in June, processed and paid for, the entry made is Expense Dr; Cash Cr. The net effect of these transactions is - Outstanding expense Dr; Cash Cr. For the month of May, expenses booked and liability for payable created. In the month of June payable paid.

There are two types of reversal entries which are as follows:-

Auto Reversal: The ERP system automatically reverses the accrual and deferral entries.

Manual Reversal: reversals are done manually.

High or Medium Critical

Another way of categorizing entries is by identifying them with their degree of criticality to the entire accounting process. These can be

Highly Critical: These are normal entries with (a) high Value or (b) they could be having an impact on Multiple Units or have (c) Statutory / Tax implication.

Medium Criticality: These are normal entries with (a) low value or (b) entries which do not have any tax or statutory impact.

Balance Sheet and /or Profit & Loss (P&L) impact

Balance Sheet entries: These are entries that would impact the Balance Sheet on both sides Typical examples of these would be (a) Inter Unit settlements or (b) reclassification of any debit balances in payables as receivables or (c) Reclassifying Credit Balances in Bank Accounts as Short Term Loans

P&L entries: These are entries which would impact the P&L on both sides. Typical examples of such entries are (a) Reclassification of Expenses or Income to correct an earlier error.

We can have a last case where we have entries that impact both — the balance sheet as well as the P&L account -such as provision for Doubtful AR; Depreciation Expense etc.

Usual or Extraordinary

Usual are those entries which can be expected in a normal running of business. Examples of these are salary expense, annual maintenance charges, provision for credit risk (doubtful debtors or AR)

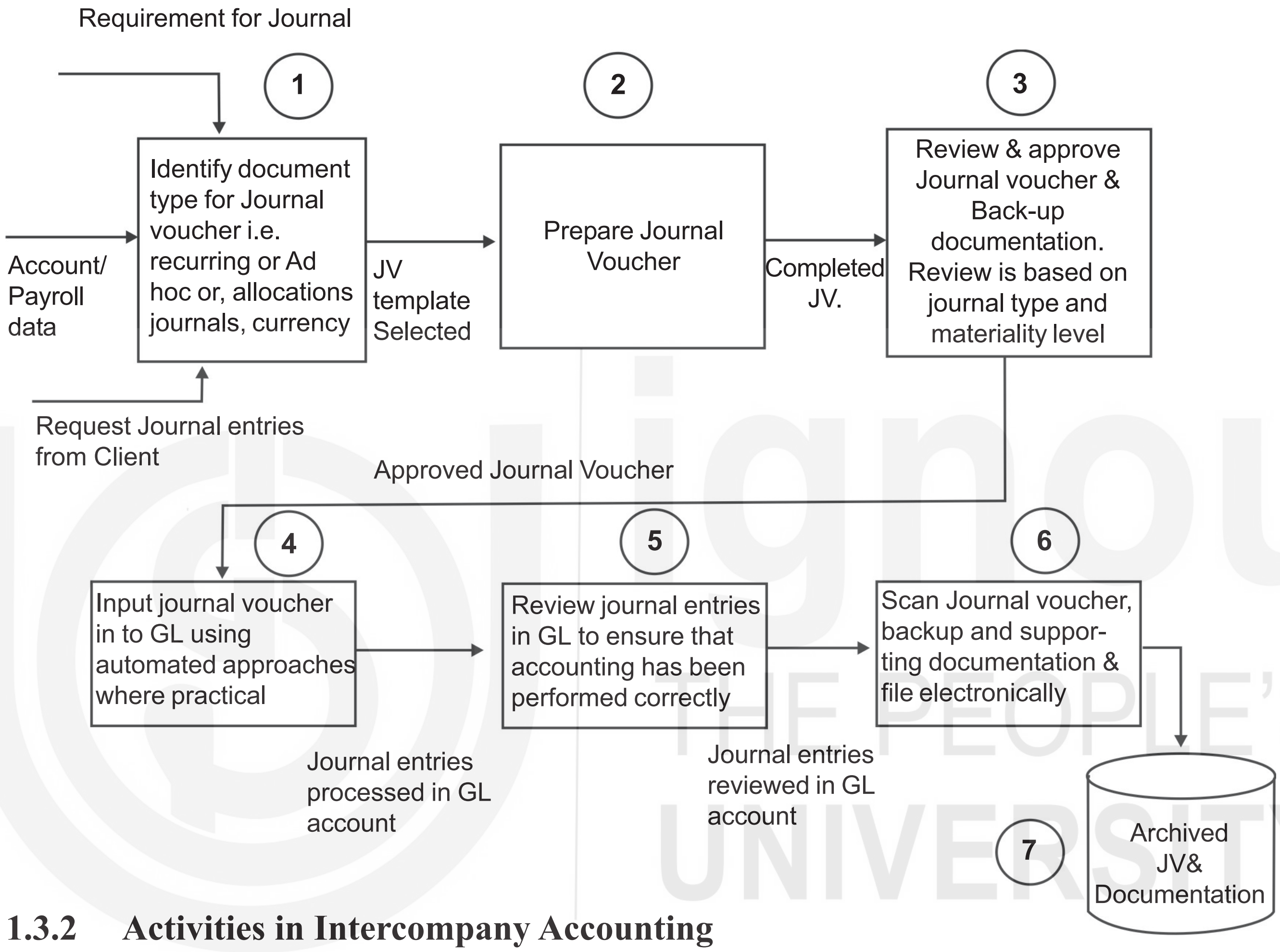
Extraordinary are those entries which ar not expected in the normal running of the business. For e.g. provision for Expenses on Employee Retrenchment or pertaining to Mergers and Acquisitions.

3. <u>**The Communication & Control Stage**</u>

As part of the control system regular quality checks are performed. Errors are notified and corrected. Finally the GL is reviewed for errors or any mistakes that could have slipped through.

Step by step diagrammatical representation of the R2R process

Journal Voucher (JV) Processing



1.3.2 Activities in Intercompany Accounting

In any large organisation there are various units (Including HO) within the group. These various units transact between themselves besides transacting with the rest of the market. Thus we can say that, Inter Company accounting is the accounting that happens between the various units within an accounting period. From a broader perspective, the following steps take place:

Step 1: The various transactions between these units are recorded Entries are made in the books of respective companies.

Step 2: Intercompany accounts statements are generated at the end of accounting period depicting all the transactions and their respective values.

Step 3: These statements are shared between the units. The inter-company accounting process starts here. In the process, the first activity is to identify and match the relevant transactions. They are checked for completeness and correctness. If they are correct, they are passed. In case there is a discrepancy or mismatch in any of the transactions, it is-put up for sorting of the exceptions. Once the exception is resolved, the entry is posted.

1.3.3 Activities in Fixed Asset Accounting

In business and accounting, Assets mean anything owned by a company (all tangible and intangible property), that can be converted into cash. **Fixed asset**, (also known as property, plant, and equipment (PP&E) in the USGAAP) are assets that cannot easily be converted into cash. Examples of such fixed assets are land and building, plant and machinery at the factory or office fixtures and furniture. All these assets attract a particular rate of depreciation (reduction in the value of an asset due to usage etc). The books where the details of the fixed assets are recorded are the **GL** and the **Fixed Assets ledger**. The GL holds the asset ledger accounts and Accumulated Depreciation Accounts for reporting in the Balance Sheet. It also includes the Depreciation Expense Accounts for reporting in the Income Statement. While the Fixed Assets ledger holds all the individual details of the asset along with all the financial history about the assets from the time a particular asset was brought by the organisation to the time it becomes non functional and is disposed off.

The accounting of these assets is done by the R2R team. The steps therein are as follows:

Step 1: Installation and Capitalization - Accounting starts at this stage. Till the asset is installed and ready for use, it is recorded as Work-in-process. Once, it is installed and ready to put into use, they are categorized as Fixed Assets. The process of recording the asset in books is known as 'Capitalization'. The cost at which the asset is recorded is the historical cost including all the expenses incurred to install the asset and to make it ready to use.

Step 2: Providing depreciation- Depreciation requirement starts running as soon as the Asset is ready for use. Essentially involves writing off the asset to the Profit and Loss in order to provide for its replacement at the end of its useful life.

Step 3: Accounting for improvements and revaluation: Maintenance expenses are incurred on an asset to ensure that it stays in good working condition. They are expensed in the year in which they are incurred. Any expenditure on an asset, which enhances its performance and productivity, is referred to as Improvement. It needs to be added to the historical cost of the asset.

Revaluation refers to an increase in the value of an asset in books. The gain as a result of this increase in the asset value is taken to the revaluation reserve/surplus. The revaluation reserve is a capital reserve in nature, not available for distribution as dividends. While an upward revaluation is permissible in India and UK, it is not allowed in the US.

Step 4: Accounting for disposal- Disposal refers to the final discarding of the asset after the end of its useful life. All related balances- the book value of the asset and the associated depreciation are brought to nil and the resultant gain/loss is taken to the Profit and Loss account.

1.3.4 How R2R Discrepancies Arose?

There is a need for reconciliation in all aspects of the business, whether it is reconciling our books with our customers or suppliers or Intercompany. Thus it is a very important aspect in the R2R cycle. There are two main teams in any organization which do the reconciliation.

These are **(a) the controllership team** (this is the team that signs off any exception resolution) and **(b) The Processing team** (this is the team which does the execution of the process of reconciliation).

Also there are two types of reconciliation process that are normally used in a large organization which are as follows:-

Tick & Tie Contra Matching Reconciliations

Schedule Based Verification Reconciliations

- **Steps in the Tick & Tie Contra Matching Reconciliations**

Step 1: The Processing team lists out the Balances that need to be justified.

Step 2 : The Processing team then justifies the matching on the basis of available knowledge that they have. In case they are in doubt they would query the concerned department to be able to substantiate their actions.

Step 3: The reconciled accounts are closed and the interim lists of unexplained balances or Transactions are sent by the processing team to the controllership team.

Step 4: Explanation /Justification to Queries are resolved. Validate Inputs are obtained, agreed upon and if considered appropriate closed out. Final List of Non Reconciled Balances to the controllership to take action.

Step 5: This is an iterative/frequent exercise and the reconciliation process is run many times before it is completely reconciled.

- **Steps in the Schedule Based Verification Reconciliations**

Step 1: The Processing team lists out the balances that need to be justified

Step 2: The balances are justified based on the information or knowledge available to the processing team. In case additional information is required the queries are sent to the concerned departments.

Step 3: The reconciled accounts are closed and the interim list of unexplained balances or transactions, known as open/non-reconciled items, is sent by the processing team to the controllership team.

Step 4: Explanation /Justification to queries is obtained from the controllership team. Validated inputs are obtained against open items and if considered appropriate, these items are closed out. The Final List of open items is given to the controllership for action.

Step 5: This is an iterative/frequent exercise and the reconciliation process is run many times before all the open items are completely reconciled.

1.3.5 Steps in Cash and Banking Management

You all are aware of the reason why companies have bank accounts and what their functions are. You will learn about bank reconciliations (Unit 3). So, here we will briefly discuss what steps an R2R team performs to manage the bank and cash operations.

The two main operational players are (a) the processing team in the organization and (b) the Bank.

Step 1: The input into this process is the bank statement.

Step 2: The processing team matches all the entries on the basis of the information in the bank statement. The processing team raises queries for all entries that are not matching. Please note that the responsibility of the team is to locate and highlight the errors in Bank Account or Bank Statement.

Step 3: The reconciled accounts are closed and the interim list of unexplained balances or transactions is sent by the processing team to the controllership team.

The suggested approach for handling these unexplained balances is:

a) Identify and define the problem and communicate the open items immediately

b) Prioritize the Oldest and high value items

c) Measure and analyze the gaps: Root Cause Analysis

d) For new type of errors: Ask - How do others resolve such issues?

e) Leverage the learning in other Bank Accounts

Step 4: Explanation / Justification to queries is obtained from the controllership team. Validated inputs are obtained against open items and if considered appropriate, these items are closed out. The Final List of open items is given to the controllership for action.

Step 5: This is an iterative/frequent exercise and the reconciliation process is run many times before all the open items are completely reconciled

Note: Remember that Bank Reconciliation is not an Account. While making a Bank Reconciliation we are not passing entries. Although as an outcome we may need to pass some entries to resolve open items. It is only a Management Information System (MIS) that serves as a thread between outputs from two different ledgers

1.3.6 Steps for Period Close and Consolidated

From purely an accounting perspective, Period Closing would entail the following activities:-

The first activity is to pass all the required journal entries. At Period Ends, some entries are passed to ensure compliance with Matching / Accrual concept. This is followed by ensuring all entries from General Journals and Sub Ledgers (Fixed Asset, Accounts Payable, and Accounts Receivable) are captured in the main GL. **The next step** is to create the Trial Balance balancing all the Asset / Liability/ Expense / Income Accounts. The Profit & Loss Account statement is made where all the Incomes and Expense Accounts are transferred, followed by the preparation of the Balance Sheet in the required format showing the period end value of the Asset and Liability Accounts.

Closing - Meaning:

Sequence of:

- Planning period close calendar

- Posting sub-systems to main General Ledger
- Analyzing General Ledger for adequacy of accruals & reversals
- Posting of manual journal entries where required and
- Finally Creating the period end trial balance which will be the basis for Balance sheet, Income statement and Cash flow.

Closing: Importance

- Timely closing of books
- Accuracy and completeness of financial data

What can GL allow you to do?

- Maintain separate companies' financial information regardless of the currency or chart of accounts.
- Administer security rules to allow only those authorized to retrieve needed accounting information.
- Produce consolidated financial reporting
- Separate cost allocation to many different ledger accounts using a single formula
- Consolidate different sets of books into a consolidated set of books & Use multiple currency rates for different companies with the organization.

The GL module is the heart of the accounting system. Detailed to summary level activity of accounts and sub accounts are maintained here. The central task of GL accounting is to provide a comprehensive information for communicating with the internal and external stakeholders

Ask yourself for Closure of Books

- How do I perform consolidation of general and subsidiary ledgers?
- How do I maintain general ledger?
- How do I generate trial balance at business segment and corporate level?
- How do I perform lease or inventory or foreign exchange transaction accounting?

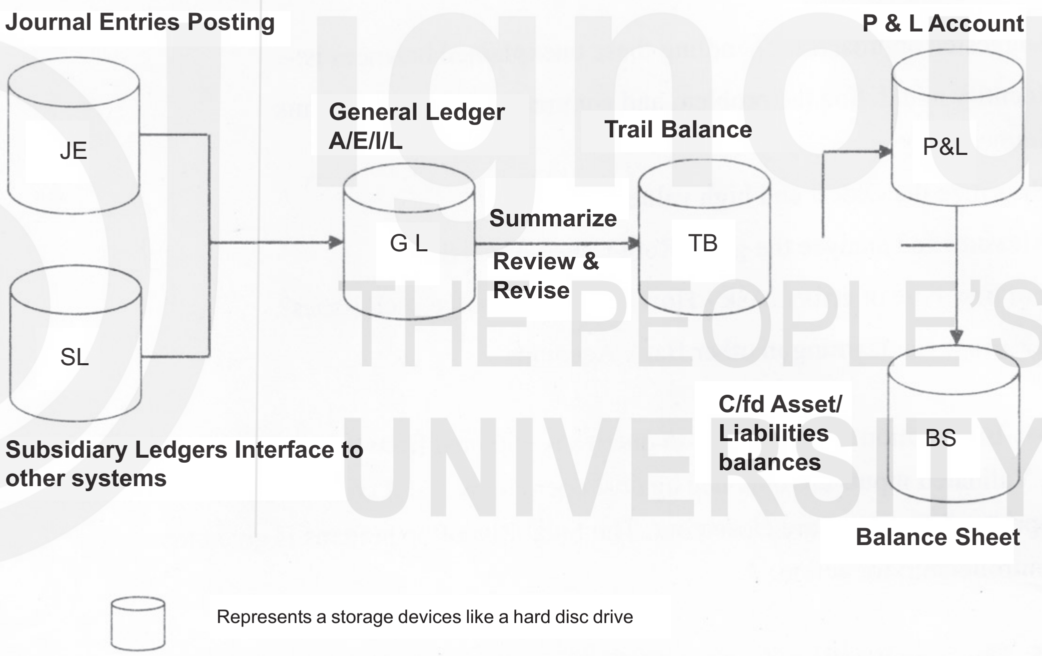
Closing calendar

Closing calendar may be called as Schedule of activities to be performed during close periods. It may be monthly / quarterly closing or fiscal year end closing. It is a list of activities to be performed during the month end closing. A stringent schedule is required to be maintained for completion of timely review, analysis and to ensure financials are fairly stated and reported. This is critical to achieve timely month end close. There are day wise activities start with pre-close. Ledger is closed for all activities at the close of business on the last day of closing which is communicated to all concerned. Example of close calendar is as below:

Month End Activity

Serial No	Day	Activity	Journal Voucher No	Source	Transaction Type
1		Tax Recon			
2	1	Freight Correction			
3		Month End Discount			
4		Claims Write Off			
5		Stock Transfer			
6		Reclass			
7	2	Accrual			
8		COGS-GL Balance			
9		Intercompany Expense			
10		EDI Expense			
11		Reclass price Load			
12	3	Overhead Report			
13	4	Production Planning Allocation			
14	5	Close Profit			

Diagrammatically we would represent it as follows:



Preparation for Period Close

Ensuring the following would ensure a smooth period close:

a) **Robust Interface Mechanism:** Start from the posting from General Journals and Subsidiary Ledgers into the GL. We must have robust interface mechanisms to ensure that data has reached the right place before commencing the period close process.

b) **Normal Account Balances:** Though while summarizing from GL to Trail Balance, we have to follow simple procedure of picking up & listing closing balance, it must be ensured that the Assets and Expenses must have Debit Balances. Liabilities and Incomes must have Credit Balances.

c) **Ledger Scrutiny and Trial Balance Review:** A Trial Balance provides a useful opportunity to compare the numbers with a prior period. Teams that are preparing the Trial Balance need to carry out variance analysis keeping in mind various errors that could be there such as Errors of Principle or the Errors of Omission or Commission. Focusing on Ledger Scrutiny is also very useful. It is very important to find the root cause of the error and making subsequent rectifications. These could be in

a) Journal Entries

b) Sub Ledgers

Thus the steps/phases in the Period close and Consolidation process are:

Planning Phase

Step 1: The first step is to well plan the process. Here the closing team would define the process along with the expected control.

Step 2: The period close team then assigns responsibility for overall ownership of the Close process

Step 3: The third step is to make & circulate Period-end guidelines and policies including the Closing timetable or calendar that would he followed.

Execution Phase 1

Once the teams are defined and the policies well understood by the team members, the next step is to execute the Period-End Accounting Transactions. As mentioned earlier these are from updating Journals and Sub Ledgers to closing the books.

Step 4: Period-end System Runs is executed. These would include the closure of the following for that period:

- Fixed Asset Depreciation
- Cost / Profit Centre allocations
- Inter-company settlements

Step 5: This is followed by evaluating and passing manual journal entries for the following:-

- Month-end Accruals
- Receipts in Advance
- Prepaids etc.

Step 6: Preliminary Close at the Unit / Legal entity level. Here the team would be closing the sub-ledgers and the GL.

Step 7: Preliminary Review of the Business Unit or Legal Entity results. This step would involve the preparation and post adjustments in Unit Ledgers as required

Step 8: Preliminary Consolidation is carried out. Gaps, if any, are identified. Adjustments are done, documented and posted.

Step 9: Second level review and approval of the consolidated financial results.

These results are then sent to the top level for approval and vindication.

Preparation for Audit

The process for a specific audit will depend on what type of audit is being performed. It begins with notification for the purpose of audit, schedule of audit and initial meeting. Being prepared for the annual audit will not only assist the auditors, but it will also ensure that you have a better understanding of your job and increase your value to your organization. Audit process will be successful in analyzing and evaluating accounts only through preparation, coordination and cooperation among the teams involved in the audit. Time frame suits to staff and auditor is agreed at the initial meeting.

Preparation includes:

- Discuss Audit procedure.
- Timing of engagement
- Determine contact people for specific areas.
- Documents for addition/deletion of fixed asset, inclusion of major new vendors/customers and any other documents which have significant impact at the financials.
- Reconcile GL accounts in advance.
- Explanation for significant variation in actual to budget
- Prior period variance etc.

To run the audit process smoothly the auditor should focus on important aspects before commencing an audit.

- Scope of duties.
- Letter of engagement
- Knowledge about Business, Accounting System, and Technical Detail.
- List of documents or schedule required for audit purpose along with instructions.

1.4 R2R - IMPORTANCE TO BUSINESS

R2R is an essential and integral part of any business seeking financial success. Recording and Reporting build the historical data of an organization's business activities over time. The accuracy and quality with which these processes are accomplished affects the organization's ability at building business credit and financial success. It is through this tool, that the public, investors, creditors, government agencies, tax agencies and employees come to know of the worth of the business.

It is important for both internal and external users.

Within the company, it becomes a necessity because of the following reasons:

- Basis of formulating budgets
- Required for internal audits
- Is an important source of information for stake holders
- Measuring current performance against past performances
- Means of making amends if any, judging from past experiences
- Gives a clear picture of the financial standing of the business, increasing employee expectations of returns.

- Means of providing information to policy makers to create and implement plans
- Aids in determiirmg areas of deficiency, thus helping in cutting costs.

For external users too, financial accounting and reporting is of extreme importance:

- Gives a clear picture of the financial standing of the business to potential investors, helping them in deciding whether or not to invest in a particular firm
- Gives adequate information to existing investors about the future of their investments
- The financial statements are the main criteria for creditors to take decisions about extending credit to firms
- Financial statements are a mandatory tool for tax agencies and are required for external audits

Companies spend hundreds of dollars in setting up account departments for dealing with the preparation of financial reports. Setting up a reliable financial accounting team is not only time consuming but also expensive. Financial accounting and reporting should be carried out by an experienced accounting team, which completes all accounting needs from start to finish. From making profit and loss accounts, trial balances and balance sheets to carrying out audits. With strong R2R team in place, an organization's leaders are able to invest their time and effort in other aspects of the business, taking a great deal of pressure off themselves in performing painstaking accounting procedures because this specialized team does that for them in the shortest times span, giving them accurate and prompt results. At any given point in time, the leaders would be able to pull up all information about the company's assets, liabilities, incomes, expenses, gains and losses. R2R consultants would give detailed reports that leaders would be able to comprehend completely, affording them a bird's eye view of the company's financial structure and standing. Financial statements form the basis of financial decisions. Thus, by providing financial services as and when they want them, R2R allows them to run their business the way they want, at the same time enabling them to keep complete control of the enterprise's resources.

Services that can be provided by R2R include:

- Providing guidance for generating files and managing accounting records such as sales invoices, statements and payments etc.
- Managing monthly or quarterly accounts
- Preparing annual profit and loss account and balance sheet
- Budgeting and cash flow forecasting
- Providing quarterly reconciliation of VAT accounts and producing VAT return
- Keeping financial records and paperwork up to date
- Managing accounts receivable in the perfect manner
- Managing accounts payable
- Maintaining management accounting details

- Regular reconciliation of accounting records
- Expert accounting help can add more value to any business.

In the outsourcing world, an F&A professional cannot be ignorant of the U.S. securities laws, particularly the Sarbanes-Oxley Act (SOX) enacted in July 2002 which reaffirmed in various “titles” the importance of accounting and accountants to corporate financial reporting and corporate governance. The law does not impend on lawyers and consultants but on accountants. Accounting (and the use of accounting principles in corporate, social and public sector financial reporting) has become very sophisticated, as business and financial markets innovate and create even more complex ways to go to market. Capitalist economies require companies to be transparent by providing accurate, reliable and relevant information to the investor citizens.

1.5 TECHNOLOGY USED IN RECORD TO REPORT PROCESS

In R2R the technology used are various Enterprise Resource Planning (ERP) software. ERP software is software that most large organisations use to carry out the recording and managing their commercial. Through this ERP, organisations can manage their business more efficiently and accurately. ERP software packages are normally many commercial software packages which are integrated into one large package. Thus any good ERP package would have Finance, Inventory, Material Management. Supply chain management, Human resources and Payroll Project management etc. The way any ERP is designed that it uses a common database and is seamlessly integrated with all its modules.

In the R2R world, any ERP package which has a financial module can be used as the technology for R2R. In large BPO’s the popular ERP’s are as follows:

SAP R/3

This is one of the most popular packages that large organisations use and BPO’s are not any exceptions. SAP stands for Systems, Applications, and Products. SAP has two modules called which are extensively used in the R2R these are as follows:-

- Financial Accounting (Fl)
- Controlling (CO)

Both these module help in carrying out the entire process of R2R through these two modules.

Oracle Financials

The other popular technology tool used for the purpose of R2R is Oracle Financials. The Oracle Financials ERP package has a complete suite of all the accounting and reporting packages build in. These are such as:

- Oracle Payables
- Oracle Receivables
- Oracle General Ledger
- Oracle Cash Management

- Oracle Assets

This complete suite allows the BPO to work smoothly to create all the vouchers, close the books of account and take out all the financial statements.

Normally the ERP is installed at the client site and the BPO accesses these modules through dedicated communications lines (as discussed in Unit I of Course 1)

Oracle Hyperion Financial tool

Lastly, another very popular tool which is used in report is the Oracle Hyperion tool. In any large organisations financial data comes from various different sources as large organisations have many companies that form part of the group. These various companies have different accounting systems or different financial closing calendars or their accounting is in different currencies. All these have to be consolidated and final group financial statements have to be generated. For the purpose, these BPO use Hyperion system which allows them to quick close and consolidate these accounts.

1.6 WHY IT IS OUTSOURCED?

‘Recording’ that is Financial Accounting and ‘Reporting’ is very important to any organisation. It is the nerve centre for all the financial transactions of the organisation. As finance is dealing with money, any misrepresentation of facts in this would only lead to loss of faith for the organisation and could even damage their reputation in the long run. Thus we see that R2R as an activity plays a very critical role in building the organisations long term relations with its customer, suppliers, bankers, other lender and all others they are dealing with.

At the same time, R2R can be a confusing and highly time consuming process. Outsourcing accounting and bookkeeping services will help an organization in cutting down costs and diverting resources to other core organizational objectives. If this R2R is being outsourced then the vendor who it is outsourced to should be equally aware of this fact. An organization has to be very careful in selecting the right partner to outsource this business.

Some of the main reasons why the R2R function is outsourced are as follows:

1. **Strong Educational Base:** This is perhaps the main reason why global want to outsource their R2R work to BPO’s in India. In India we have a very strong educational system which produces a large base of chartered accountants and commerce graduates who are well versed with the process of R2R. This is coupled with the fact that this base also has good communication skills especially in English language.

2. **Cost Arbitrage:** The second main reason is that having this process in India has a very huge cost advantage. Cost for these accountants in India for specialized skills is much lower than that in the western world.

3. **Managerial Skill:** BPO’s in India ensure that they have necessary resources with adequate knowledge and good managerial skills to manage the entire R2R process. This is not so relevant in the lower end simple processes such as O2C, P2P that are outsourced as they are technology intensive. However, when a process such as R2R is outsourced it requires decision making managerial

skills. The BPO is required to manage expectations, on behalf of the client, of multiple stakeholders both external and internal. Thus managerial skill availability is an important factor for outsourcing.

Check Your Progress

1 **Fill up the blanks:**

a) The_____________Act was enacted in 2020.

b) Financial Accounting is the basis of_______.

c) Financial decisions are based on______________.

d) New capitalists require companies to be ___________.

e) Availability of __________ is important for outsourcing.

2 **State whether the statements are True or False**:

a) Outsourcing accounting and bookkeeping services helps in cost cutting.

b) Management accounting acts as an important source of information for stake holders.

c) The R2R function is the main criteria for creditors to take decisions about extending credit to firms.

d) Setting up a reliable financial accounting team is a time consuming activity.

e) Cost for these accountants in India for specialized skills is higher than those in the western world.

1.7 LET US SUM UP

R2R stands for Record to Report. Recording all the financial transactions in its day books which would be followed by posting them in the respective ledgers and making the trial balance followed by the Profit and Loss and the Balance sheet is known as recording where as Reporting is a process, wherein financial data that has been captured during the fixed period of time (Monthly/quarterly/annually) is presented to all the external and internal stakeholders based on certain requirements.

There is large global group which have smaller companies within them. These companies operate as individual entities and they are responsible for their own P&L. IBM, Pfizer, General Motors are some examples of large global groups. Financial, Tax regulatory and management are the three broad categories of reporting. There are varied users of reporting but presenting the financial numbers to the Stock Markets is a very important aspect of reporting. On the basis of financial reporting, tax and regulatory reporting is done. Management reporting is the last group or users of financial reporting and such reporting is used to make decisions which are both strategic and operational in nature. There are lots of errors that happen on the production floor which can be either due to time, accuracy or any other reasons due to operational issues.

R2R has been outsourced to India due to various reasons such as cost effectiveness, managerial skills, strong domain knowledge etc.

1.8 ANSWERS TO CHECK YOUR PROGRESS

1 a) Sarbanes Oxley (SOX)

b) Formulating budgets

c) Financial statements

d) Transparent

e) Managerial skills

2 a) True b) False c) False d) False e) False

1.9 TERMINAL QUESTIONS

1) Why is it required to reverse the entries? Explain the types of reversal entries?
2) Provide an example of an entry impacting the balance sheet and P&L account?
3) Why is it important to record the transactions properly?
4) There are integral functions in any business which helps to get the financial success". Explain.
5) Do you think outsourcing R2R function has been beneficial for India?