

ENTITY NAME: _____

DEBT AND LEASE OBLIGATIONS

We need to understand:

- How and by whom the transactions are initiated
- The accounting processing involved from initiation of a transaction to its inclusion in the general ledger or financial statements, including how the computer is used to process data
- The supporting documents involved, including accounting records and journals, source documents, and electronic means involved in the processing of the transactions
- The documents and reports generated by the accounting system

SECTION A

INTERNAL CONTROL OBJECTIVES

- Debt and lease obligations and related expenses are authorized and recorded correctly as to account, amount, and period.
- Requirements and restrictions imposed by debt covenants and lease agreements are complied with and monitored.
- Debt retirements and modifications have been properly accounted for.
- Debt instruments and lease agreements are adequately safeguarded.

POTENTIAL ERRORS AND FRAUD

- The entity becomes obligated for debts that are not properly authorized or that are taken on at unfavorable terms.
- Long-term or short-term debt is misclassified.
- Pledged assets or collateral are not identified and disclosed; unauthorized pledging of assets occurs.
- Violations of debt covenants or lease agreements result in default.
- Capital leases are recorded as operating leases or vice versa.
- Interest expense is recorded in the wrong period or at the wrong amount, is not recorded, or is misclassified.
- Debt proceeds are used for other than appropriate purposes.

UNDERSTANDING OF ACCOUNTING SYSTEM

1. How and by whom are the transactions initiated?

2. Describe the source documents that support the transactions.

3. Describe the computer media that is used in the processing of accounting information.

4. Describe the documents and reports generated by the accounting system.

5. Describe the accounting processing, records, and files (including how frequently they are updated) that are used to process the transactions, including how transactions are reflected in journals of original entry and in the general ledger.

SECTION B

FURTHER UNDERSTANDING OF CONTROL ACTIVITIES

	Yes	No	N/A
1. Do borrowings and leases require authorization by designated personnel?	_____	_____	_____
2. Are signatures of two or more designated officials required on all notes payable, lease agreements, and renewals?	_____	_____	_____
3. Do paid notes get canceled and returned?	_____	_____	_____
4. Are interest charges regularly posted and reviewed?	_____	_____	_____
5. Is compliance with loan covenants and lease agreements periodically reviewed and monitored?	_____	_____	_____
6. Are detailed records periodically reconciled with the general ledger control accounts?	_____	_____	_____
7. Are debt instruments and related legal documents (e.g., notes, bonds) adequately safeguarded?	_____	_____	_____