# CHAPTER 8
INTERNAL CONTROL AND CASH

## SUMMARY OF QUESTIONS BY STUDY OBJECTIVES AND BLOOM’S TAXONOMY

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**Multiple Choice Questions**

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**Brief Exercises**

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supg This question also appears in the Study Guide.

sup This question also appears in a self-test at the student companion website.
### SUMMARY OF QUESTIONS BY STUDY OBJECTIVES AND BLOOM’S TAXONOMY

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### SUMMARY OF STUDY OBJECTIVES BY QUESTION TYPE

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SUMMARY OF STUDY OBJECTIVES BY QUESTION TYPE

| Study Objective 7 | 26. TF 111. MC 119. MC 127. MC 153. BE 170. Ex 178. Ex |
| 27. TF 112. MC 120. MC 128. MC 154. BE 171. Ex 179. Ex |
| 38. TF 114. MC 122. MC 130. MC 156. BE 173. Ex 195. C |
| 109. MC 117. MC 125. MC 133. MC 159. BE 176. Ex |
| 110. MC 118. MC 126. MC 146. MC 169. Ex 177. Ex |
| Study Objective 8 | 29. TF 30. TF 134. MC 135. MC 136. MC 147. MC |

Note: TF = True-False       BE = Brief Exercise       C = Completion
       MC = Multiple Choice    Ex = Exercise

The chapter also contains one set of fifteen Matching questions and five Short-Answer Essay questions.

CHAPTER STUDY OBJECTIVES

1. Define internal control. Internal control is the related methods and procedures adopted within an organization to safeguard its assets and to enhance the accuracy and reliability of its accounting records.

2. Identify the principles of internal control. The principles of internal control are: establishment of responsibility; segregation of duties; documentation procedures; physical, mechanical, and electronic controls; independent internal verification; and other controls, such as bonding and requiring employees to take vacations.

3. Explain the applications of internal control principles to cash receipts. Internal controls over cash receipts include: (a) designating specific personnel to handle cash; (b) assigning different individuals to receive cash, record cash, and maintain custody of cash; (c) obtaining remittance advices for mail receipts, cash register tapes for over-the-counter receipts, and deposit slips for bank deposits; (d) using company safes and bank vaults to store cash with access limited to authorized personnel, and using cash registers in executing over-the-counter receipts; (e) making independent daily counts of register receipts and daily comparing total receipts with total deposits; and (f) bonding personnel that handle cash and requiring them to take vacations.

4. Explain the applications of internal control principles to cash disbursements. Internal controls over cash disbursements include: (a) having specific individuals such as the treasurer authorized to sign checks; (b) assigning different individuals to approve items for payment, pay the items, and record the payment; (c) using prenumbered checks and accounting for all checks, with each check supported by an approved invoice; (d) storing blank checks in a safe or vault with access restricted to authorized personnel, and using a checkwriter to imprint amounts on checks; (e) comparing each check with the approved invoice before issuing the check, and making monthly reconciliations of bank and book balances; and (f) after payment, stamping each approved invoice PAID.
5. **Describe the operation of a petty cash fund.** Companies operate a petty cash fund to pay relatively small amounts of cash. They must establish the fund, make payments from the fund, and replenish the fund when the cash in the fund reaches a minimum level.

6. **Indicate the control features of a bank account.** A bank account contributes to good internal control by providing physical controls for the storage of cash. It minimizes the amount of currency that a company must keep on hand, and it creates a double record of a depositor's bank transactions.

7. **Prepare a bank reconciliation.** It is customary to reconcile the balance per books and balance per bank to their adjusted balances. The steps in the reconciling process are to determine deposits in transit, outstanding checks, errors by the depositor or the bank, and unrecorded bank memoranda.

8. **Explain the reporting of cash.** Companies list cash first in the current assets section of the balance sheet. In some cases, they report cash together with cash equivalents. Cash restricted for a special purpose is reported separately as a current asset or as a noncurrent asset, depending on when the cash is expected to be used.

**TRUE-FALSE STATEMENTS**

1. Internal control is mainly concerned with the amount of authority a supervisor exercises over a subordinate.

2. A highly automated computerized system of accounting eliminates the need for internal control.

3. The safeguarding of assets is an objective of a company's system of internal control.

4. Management is responsible for establishing a system of internal control.

5. Internal control is most effective when several people are responsible for a given task.

6. The responsibility for keeping the records for an asset should be separate from the physical custody of that asset.

7. Requiring employees to take vacations is a weakness in the system of internal controls because it does not promote operational efficiency.

8. The extent of internal control features adopted by a company must be evaluated in terms of cost-benefit.

9. An effective system of internal control requires that at least two individuals be assigned to one cash drawer so that each can serve as check on the other.

10. Only large companies need to be concerned with a system of internal control.

11. The responsibility for ordering, receiving, and paying for merchandise should be assigned to different individuals.
12. In order to prevent a transaction from being recorded more than once, a company should maintain only one book of original entry.

13. Firms use physical, mechanical, and electronic controls primarily to safeguard their assets.

14. A segregation of duties among employees eliminates the possibility of collusion.

15. For efficiency of operations and better control over cash, a company should maintain only one bank account.

16. Cash registers are an important internal control device used in controlling over-the-counter receipts.

17. Checks received in the mail should be immediately stamped "NSF" to prevent unauthorized cashing of the check.

18. Control over cash disbursements is improved if major expenditures are paid by check.

19. In a voucher system, vouchers are prepared in the accounts receivable department.

20. Electronic Funds Transfer (EFT) is a disbursement system that uses telephone or computer to transfer cash from one location to another.

21. A voucher system is used by many large companies as a means of controlling cash receipts.

22. The petty cash fund eliminates the need for a bank checking account.

23. Cash register overages are deposited in the petty cash fund and cash shortages are made-up from the petty cash fund.

24. A deposit ticket is a negotiable instrument that can be transferred to another party by endorsement.

25. If a company deposits all its receipts in the bank and pays all its bills by check, then the monthly bank statement balance will always agree with the company’s record of its checking account balance.

26. Checks from customers who pay their accounts promptly are called outstanding checks.

27. All reconciling items in determining the adjusted cash balance per books require the depositor to make adjusting journal entries to the Cash account.

28. A bank reconciliation is generally prepared by the bank and sent to the depositor along with cancelled checks.

29. Cash equivalents are highly liquid investments that can be converted into a specific amount of cash.

30. Cash which is restricted for a specific use should be separately reported.
Additional True-False Questions

31. Internal control consists of the plan of organization and all of the related methods and measures adopted within a business to (a) safeguard its assets, and (b) enhance the accuracy and reliability of its accounting records.

32. In general, documents should be prenumbered and all documents should be accounted for.

33. Collusion may result when one individual circumvents prescribed controls and may significantly impair the effectiveness of a system.

34. Personnel who handle cash receipts should have the option of taking a vacation or not.

35. The duties of approving an item for payment and paying the item should be done by different departments or individuals.

36. The custodian of the petty cash fund has the responsibility of recording a journal entry every time cash is used from the fund.

37. A debit memorandum could show the collection of a note receivable by the bank.

38. To obtain maximum benefit from a bank reconciliation, the reconciliation should be prepared by an employee who has no other responsibilities pertaining to cash.

Answers to True-False Statements

|------|------|------|------|------|------|------|------|------|------|------|------|------|------|

MULTIPLE CHOICE QUESTIONS

39. Which one of the following is not an objective of a system of internal controls?
   a. Safeguard company assets
   b. Overstate liabilities in order to be conservative
   c. Enhance the accuracy and reliability of accounting records
   d. Reduce the risks of errors

40. Internal controls are concerned with
   a. only manual systems of accounting.
   b. the extent of government regulations.
   c. safeguarding assets.
   d. preparing income tax returns.
41. The Foreign Corrupt Practices Act requires that all U.S. corporations under the jurisdic-
tion of the Securities and Exchange Commission
   a. have at least one foreign subsidiary.
   b. maintain accounting records of foreign branches and subsidiaries in the local foreign
currency.
   c. maintain an adequate system of internal control.
   d. must file reports with the National Commission on Fraudulent Financial Reporting.

42. Internal control is defined, in part, as a plan that safeguards
   a. all balance sheet accounts.
   b. assets.
   c. liabilities.
   d. capital stock.

43. The importance of a good system of internal controls was recognized with the passage of
   a. the Securities and Exchange Act of 1933.
   c. the Blue Sky Laws.

44. Companies that are subject to, but fail to comply with, the Foreign Corrupt Practices Act of
   1977
   a. may do so legally by obtaining an exemption.
   b. will be automatically dissolved.
   c. may be subject to fines and officer imprisonment.
   d. may be forced to sell their foreign subsidiaries.

45. Internal controls are *not* designed to safeguard assets from
   a. natural disasters.
   b. employee theft.
   c. robbery.
   d. unauthorized use.

46. Having one person post entries to accounts receivable subsidiary ledger and a different
   person post to the Accounts Receivable Control account in the general ledger is an
   example of
   a. inadequate internal control.
   b. duplication of effort.
   c. external verification.
   d. segregation of duties.

47. Having one person responsible for the related activities of ordering merchandise,
   receiving goods, and paying for them
   a. increases the potential for errors and fraud.
   b. decreases the potential for errors and fraud.
   c. is an example of good internal control.
   d. is a good example of safeguarding the company's assets.
48. The custodian of a company asset should
   a. have access to the accounting records for that asset.
   b. be someone outside the company.
   c. not have access to the accounting records for that asset.
   d. be an accountant.

49. Internal auditors
   a. are hired by CPA firms to audit business firms.
   b. are employees of the IRS who evaluate the internal controls of companies filing tax
      returns.
   c. evaluate the system of internal controls for the companies that employ them.
   d. cannot evaluate the system of internal controls of the company that employs them
      because they are not independent.

50. When two or more people get together for the purpose of circumventing prescribed
    controls, it is called
   a. a fraud committee.
   b. collusion.
   c. a division of duties.
   d. bonding of employees.

51. From an internal control standpoint, the asset most susceptible to improper diversion and
    use is
   a. prepaid insurance.
   b. cash.
   c. buildings.
   d. land.

52. The principle of establishing responsibility does not include
   a. one person being responsible for one task.
   b. authorization of transactions.
   c. independent internal verification.
   d. approval of transactions.

53. The control principle related to not having the same person authorize and pay for goods is
    known as
   a. establishment of responsibility.
   b. independent internal verification.
   c. segregation of duties.
   d. rotation of duties.

54. Two individuals at a retail store work the same cash register. You evaluate this situation
    as
   a. a violation of establishment of responsibility.
   b. a violation of segregation of duties.
   c. supporting the establishment of responsibility.
   d. supporting internal independent verification.
55. An accounts payable clerk also has access to the approved supplier master file for purchases. The control principle of
   a. establishment of responsibility is violated.
   b. independent internal verification is violated.
   c. documentation procedures is violated.
   d. segregation of duties is violated.

56. Controls that enhance the accuracy and reliability of the accounting records are
   a. automated controls.
   b. external controls.
   c. mechanical and electronic controls.
   d. physical controls.

57. Related selling activities do not include
   a. ordering the merchandise.
   b. making a sale.
   c. shipping the goods.
   d. billing the customer.

58. The independent internal verification principle involves each of the following except the
    ____________ of data prepared by other employees.
   a. comparison
   b. reconciliation
   c. review
   d. segregation

59. Related buying activities include
   a. ordering, receiving, paying.
   b. ordering, selling, paying.
   c. ordering, shipping, billing.
   d. selling, shipping, paying.

60. Joe is warehouse custodian and also maintains the accounting record of the inventory held at the warehouse. An assessment of this situation indicates
   a. documentation procedures are violated.
   b. independent internal verification is violated.
   c. segregation of duties is violated.
   d. establishment of responsibility is violated.

61. Physical controls to safeguard assets do not include
   a. cashier department supervisors.
   b. vaults.
   c. employee identification badges.
   d. security guards.

62. In large companies, the independent internal verification procedure is often assigned to
   a. computer operators.
   b. management.
   c. internal auditors.
   d. outside CPAs.
63. Maximum benefit from independent internal verification is obtained when
   a. it is made on a pre-announced basis.
   b. it is done by the employee possessing custody of the asset.
   c. discrepancies are reported to management.
   d. it is done at the time of the audit.

64. If employees are bonded
   a. it means that they are not allowed to handle cash.
   b. they have worked for the company for at least 10 years.
   c. they have been insured against misappropriation of assets.
   d. it is impossible for them to steal from the company.

65. Mrs. Smith has worked for Arcco Inc., for 20 years without taking a vacation. An internal
    control feature that would address this situation would be
   a. other controls.
   b. establishment of responsibility.
   c. physical controls.
   d. documentation procedures.

66. A system of internal control
   a. is infallible.
   b. can be rendered ineffective by employee collusion.
   c. invariably will have costs exceeding benefits.
   d. is premised on the concept of absolute assurance.

67. For accounting purposes, postdated checks (checks payable in the future) are considered
    to be
   a. money orders.
   b. cash.
   c. petty cash.
   d. accounts receivable.

68. Postage stamps on hand are considered to be
   a. cash.
   b. petty cash.
   c. cash equivalents.
   d. a prepaid expense.

69. Which one of the following items would not be considered cash?
   a. Coins
   b. Money orders
   c. Currency
   d. Postdated checks

70. Checks received through the mail should
   a. immediately be endorsed "For Deposit Only."
   b. be sent to the accounts receivable subsidiary ledger clerk for immediate posting to the
      customer's account.
   c. be cashed at the bank as soon as possible.
   d. be "rung up" on a cash register immediately.
71. Proper control for over-the-counter cash receipts includes
   a. a cash register with totals visible to the customer.
   b. using electronic cash registers with no tapes.
   c. cash count sheets requiring only the supervisor's signature.
   d. cash count sheets requiring only the cashier's signature.

72. A company stamps checks received in the mail with the words "For Deposit Only". This endorsement is called a(n)
   a. blank endorsement.
   b. rubber stamp.
   c. restrictive endorsement.
   d. operational endorsement.

73. The daily cash count of cash register receipts made by department supervisors is an example of
   a. other controls.
   b. independent internal verification.
   c. establishment of responsibility.
   d. segregation of duties.

74. The use of remittance advices for mail receipts is an example of
   a. documentation procedures.
   b. other controls.
   c. physical controls.
   d. independent internal verification.

75. Allowing only designated personnel to handle cash receipts is an example of
   a. establishment of responsibility.
   b. segregation of duties.
   c. documentation procedures.
   d. independent internal verification.

76. Control over cash disbursements is generally more effective when
   a. all bills are paid in cash.
   b. disbursements are made by the accounts payable subsidiary clerk.
   c. payments are made by check.
   d. all purchases are made on credit.

77. Reconciling the bank statement monthly is an example of
   a. segregation of duties.
   b. independent internal verification.
   c. establishment of responsibility.
   d. documentation procedures.

78. An exception to disbursements being made by check is acceptable when cash is paid
   a. to an owner.
   b. to employees as wages.
   c. from petty cash.
   d. to employees as loans.
79. Allowing only the treasurer to sign checks is an example of
   a. documentation procedures.
   b. segregation of duties.
   c. other controls.
   d. establishment of responsibility.

80. Blank checks
   a. should be safeguarded.
   b. should be pre-signed.
   c. do not need to be safeguarded since they must be signed to be valid.
   d. should not be prenumbered.

81. An employee authorized to sign checks should not record
   a. owner cash contributions.
   b. mail receipts.
   c. cash disbursement transactions.
   d. sales transactions.

82. A voucher system is a series of prescribed control procedures
   a. to check the credit worthiness of customers.
   b. designed to assure that disbursements by check are proper.
   c. which eliminates the need for a sales journal.
   d. specifically designed for small firms who may not have checking accounts.

83. Under a voucher system, a prenumbered voucher is prepared for every
   a. cash receipt, regardless of source.
   b. transaction entered into by the business.
   c. expenditure except those made from petty cash.
   d. journal entry.

84. A credit balance in Cash Over and Short is reported as a(n)
   a. asset.
   b. liability.
   c. miscellaneous expense.
   d. miscellaneous revenue.

85. The entry to replenish a petty cash fund includes a credit to
   a. Petty Cash.
   b. Cash.
   c. Freight-in.
   d. Postage Expense.

86. A debit balance in Cash Over and Short is reported as a
   a. contra asset.
   b. miscellaneous asset.
   c. miscellaneous expense.
   d. miscellaneous revenue.
87. A petty cash fund of $100 is replenished when the fund contains $3 in cash and receipts for $93. The entry to replenish the fund would
   a. credit Cash Over and Short for $4.
   b. credit Miscellaneous Revenue for $4.
   c. debit Cash Over and Short for $4.
   d. debit Miscellaneous Expense for $4.

88. A petty cash fund is generally established in order to
   a. pay for all merchandise purchased on account.
   b. pay employees’ wages.
   c. make loans internally to employees.
   d. pay relatively small expenditures.

89. A petty cash fund should be replenished
   a. every day.
   b. at the end of every accounting period.
   c. once a year.
   d. as soon as an expense is paid from the fund.

90. A petty cash fund should not be used for
   a. postage due.
   b. loans to the petty cash custodian.
   c. taxi fares.
   d. customer lunches.

91. The size of the petty cash fund is dependent on
   a. the wishes of the custodian of the fund.
   b. anticipated disbursements for the year.
   c. anticipated disbursements for a three- to four-week period.
   d. the size of the regular cash account.

92. Replenishing the petty cash fund requires
   a. a debit to Cash.
   b. a credit to Petty Cash.
   c. a debit to various expense accounts.
   d. no accounting entry.

93. Entries are made to the Petty Cash account when
   a. establishing the fund.
   b. making payments out of the fund.
   c. recording shortages in the fund.
   d. replenishing the fund.

94. A $100 petty cash fund has cash of $15 and receipts of $80. The journal entry to replenish the account would include a credit to
   a. Cash for $85.
   b. Petty Cash for $85.
   c. Cash Over and Short for $5.
   d. Cash for $80.
95. A $100 petty cash fund has cash of $17 and receipts of $80. The journal entry to replenish the account would include a
   a. debit to Cash for $80.
   b. credit to Petty Cash for $83.
   c. debit to Cash Over and Short for $3.
   d. credit to Cash for $80.

96. A $100 petty cash fund has cash of $18 and receipts of $86. The journal entry to replenish the account would include a
   a. debit to Cash for $86.
   b. credit to Petty Cash for $86.
   c. credit to Cash Over and Short for $4.
   d. credit to Cash for $86.

97. All of the following are parties to a check except the
   a. bank.
   b. Federal Reserve.
   c. maker.
   d. payee.

98. When opening a bank checking account, a signature card
   a. indicates to whom money is to be paid.
   b. indicates each person authorized to sign checks on the account.
   c. is attached to all pre-printed checks.
   d. is required only when dealing with an out-of-state bank.

99. Which one of the following is not necessarily a party to a check?
   a. Maker
   b. Buyer
   c. Payee
   d. Payer

100. A bank statement
    a. lets a depositor know the financial position of the bank as of a certain date.
    b. is a credit reference letter written by the depositor's bank.
    c. is a bill from the bank for services rendered.
    d. shows the activity which increased or decreased the depositor's account balance.

101. Which one of the following would not cause a bank to debit a depositor's account?
    a. Bank service charge
    b. Collection of a note receivable
    c. Wiring of funds to other locations
    d. Checks marked NSF

102. A company maintains the asset account, Cash in Bank, on its books, while the bank maintains a reciprocal account which is
    a. a contra-asset account.
    b. a liability account.
    c. also an asset account.
    d. an owner's equity account.
103. A remittance advice attached to a company check provides
   a. details about the running cash balance in the checking account.
   b. the magnetic bank routing numbers.
   c. the explanation of the purpose of the check.
   d. the signature space for the maker.

104. A deposit made by a company will appear on the bank statement as a
   a. debit.
   b. credit.
   c. debit memorandum.
   d. credit memorandum.

105. A check returned by the bank marked "NSF" means
   a. no service fee.
   b. no signature found.
   c. not satisfactorily filled-out.
   d. not sufficient funds.

106. A debit memorandum would not be issued by the bank for
   a. a bank service charge.
   b. the issuance of traveler's checks.
   c. the wiring of funds.
   d. the collection of a notes receivable.

107. On a bank reconciliation, deposits in transit are
   a. added to the bank balance.
   b. deducted from the bank balance.
   c. added to the book balance.
   d. deducted from the book balance.

108. A bank reconciliation should be prepared
   a. whenever the bank refuses to lend the company money.
   b. when an employee is suspected of fraud.
   c. to explain any difference between the depositor's balance per books and the balance per bank.
   d. by the person who is authorized to sign checks.

109. Deposits in transit
   a. have been recorded on the company's books but not yet by the bank.
   b. have been recorded by the bank but not yet by the company.
   c. have not been recorded by the bank or the company.
   d. are checks from customers which have not yet been received by the company.

110. In preparing a bank reconciliation, outstanding checks are
   a. added to the balance per bank.
   b. deducted from the balance per books.
   c. added to the balance per books.
   d. deducted from the balance per bank.
111. If a check correctly written and paid by the bank for $428 is incorrectly recorded on the company's books for $482, the appropriate treatment on the bank reconciliation would be to
a. add $54 to the bank's balance.
b. add $54 to the book's balance.
c. deduct $54 from the bank's balance.
d. deduct $428 from the book's balance.

112. Notification by the bank that a deposited customer check was returned NSF requires that the company make the following adjusting entry:
a. Accounts Receivable
   Cash
b. Cash
   Accounts Receivable
c. Miscellaneous Expense
   Accounts Receivable
d. No adjusting entry is necessary.

113. Tolan Company had checks outstanding totaling $5,400 on its June bank reconciliation. In July, Tolan Company issued checks totaling $38,900. The July bank statement shows that $24,300 in checks cleared the bank in July. A check from one of Tolan Company's customers in the amount of $300 was also returned marked "NSF." The amount of outstanding checks on Tolan Company's July bank reconciliation should be
a. $14,600.
b. $20,000.
c. $19,700.
d. $9,200.

114. Each of the following items affect the cash balance per books except
a. bank service charges.
b. notes collected by the bank.
c. NSF checks.
d. outstanding checks.

115. Grant Company gathered the following reconciling information in preparing its July bank reconciliation:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash balance per books, 7/31</td>
<td>$5,500</td>
</tr>
<tr>
<td>Deposits in transit</td>
<td>150</td>
</tr>
<tr>
<td>Notes receivable and interest collected by bank</td>
<td>850</td>
</tr>
<tr>
<td>Bank charge for check printing</td>
<td>20</td>
</tr>
<tr>
<td>Outstanding checks</td>
<td>2,000</td>
</tr>
<tr>
<td>NSF check</td>
<td>170</td>
</tr>
</tbody>
</table>

The adjusted cash balance per books on July 31 is
a. $6,160.
b. $6,010.
c. $4,310.
d. $4,460.
116. Yenn Company developed the following reconciling information in preparing its September bank reconciliation:

- Cash balance per bank, 9/30 $15,000
- Note receivable collected by bank 6,000
- Outstanding checks 9,000
- Deposits in transit 4,500
- Bank service charge 75
- NSF check 1,200

Determine the cash balance per books (before adjustments) for Yenn Company.

a. $11,775.
b. $19,500.
c. $5,775.
d. $15,000.

117. Bank errors

a. occur because of time lags.
b. must be corrected by debits.
c. are infrequent in occurrence.
d. are corrected by making an adjusting entry on the depositor's books.

118. An adjusting entry is \textit{not} required for

a. outstanding checks.
b. collection of a note by the bank.
c. NSF checks.
d. bank service charges.

119. Jones Company had checks outstanding totaling $6,400 on its May bank reconciliation. In June, Jones Company issued checks totaling $39,900. The July bank statement shows that $29,700 in checks cleared the bank in July. A check from one of Jones Company's customers in the amount of $300 was also returned marked "NSF." The amount of outstanding checks on Jones Company's July bank reconciliation should be

a. $19,600.
b. $10,200.
c. $16,600.
d. $3,800.

120. Wilson Company gathered the following reconciling information in preparing its August bank reconciliation:

- Cash balance per books, 8/31 $7,000
- Deposits in transit 300
- Notes receivable and interest collected by bank 1,700
- Bank charge for check printing 40
- Outstanding checks 4,000
- NSF check 340

The adjusted cash balance per books on August 31 is

a. $8,320.
b. $8,020.
c. $4,620.
d. $4,920.
121. Jansen Company gathered the following reconciling information in preparing its April bank reconciliation:

- Cash balance per books, 4/30 $6,600
- Deposits in transit 900
- Notes receivable and interest collected by bank 2,220
- Bank charge for check printing 75
- Outstanding checks 4,500
- NSF check 420

The adjusted cash balance per books on April 30 is
a. $9,225.
b. $8,820.
c. $8,325.
d. $9,165.

122. Barns Company developed the following reconciling information in preparing its September bank reconciliation:

- Cash balance per bank, 9/30 $15,400
- Note receivable collected by bank 8,400
- Outstanding checks 12,600
- Deposits in transit 6,300
- Bank service charge 105
- NSF check 1,680

Using the above information, determine the cash balance per books (before adjustments) for the Barns Company.

a. $13,685
b. $21,700
c. $2,485
d. $21,000

123. In the month of November, Joles Company Inc. wrote checks in the amount of $9,250. In December, checks in the amount of $12,658 were written. In November, $8,468 of these checks were presented to the bank for payment, and $10,883 were presented in December. What is the amount of outstanding checks at the end of November?

a. $1,775
b. $782
c. $2,557
d. $3,550

124. In the month of November, Joles Company Inc. wrote checks in the amount of $9,250. In December, checks in the amount of $12,658 were written. In November, $8,468 of these checks were presented to the bank for payment, and $10,883 were presented in December. What is the amount of outstanding checks at the end of December?

a. $1,775
b. $782
c. $2,557
d. $3,550
125. At April 30, Beckett Company has the following bank information: cash balance per bank $4,600; outstanding checks $280; deposits in transit $550; credit memo for interest $10; bank service charge $20. What is Beckett's adjusted cash balance on April 30?
   a. $4,860
   b. $4,880
   c. $4,330
   d. $4,870

126. At June 30, Coulsen Company has the following bank information: cash balance per bank $3,600; outstanding checks $280; deposits in transit $550; credit memo for interest $10; bank service charge $20. What is Coulsen's adjusted cash balance on June 30?
   a. $3,860
   b. $3,880
   c. $3,330
   d. $3,870

127. Pierce Company wrote checks totaling $8,540 during October and $9,325 during November. $8,120 of these checks cleared the bank in October, and $9,110 cleared the bank in November. What was the amount of outstanding checks on November 30?
   a. $635
   b. $115
   c. $305
   d. $990

128. Rhoden Company wrote checks totaling $17,080 during October and $18,650 during November. $16,240 of these checks cleared the bank in October, and $18,220 cleared the bank in November. What was the amount of outstanding checks on November 30?
   a. $1,270
   b. $230
   c. $610
   d. $1,980

129. Perkins Company assembled the following information in completing its March bank reconciliation: balance per bank $3,820; outstanding checks $775; deposits in transit $1,250; NSF check $80; bank service charge $25; cash balance per books $4,400. As a result of this reconciliation, Perkins will
   a. reduce its cash account by $475.
   b. reduce its cash account by $25.
   c. increase its cash account by $55.
   d. reduce its cash account by $105.

130. Reisner Company assembled the following information in completing its July bank reconciliation: balance per bank $11,460; outstanding checks $2,325; deposits in transit $3,750; NSF check $240; bank service charge $75; cash balance per books $13,200. As a result of this reconciliation, Reisner will
   a. reduce its cash account by $1,425.
   b. reduce its cash account by $75.
   c. increase its cash account by $165.
   d. reduce its cash account by $315.
131. If a check correctly written and paid by the bank for $491 is incorrectly recorded on the company's books for $419, the appropriate treatment on the bank reconciliation would be to
   a. add $72 to the book's balance.
   b. subtract $72 from the book's balance.
   c. deduct $72 from the bank's balance.
   d. deduct $491 from the book's balance.

132. In the month of May, Klein Company Inc. wrote checks in the amount of $27,750. In June, checks in the amount of $37,974 were written. In May, $25,404 of these checks were presented to the bank for payment, and $32,649 in June. What is the amount of outstanding checks at the end of May?
   a. $5,325
   b. $2,346
   c. $7,671
   d. $10,650

133. In the month of May, Klein Company Inc. wrote checks in the amount of $27,750. In June, checks in the amount of $37,974 were written. In May, $25,404 of these checks were presented to the bank for payment, and $32,649 in June. What is the amount of outstanding checks at the end of June?
   a. $5,325
   b. $2,346
   c. $7,671
   d. $10,650

134. Cash equivalents include each of the following except
   a. bank certificates of deposit.
   b. money market funds.
   c. petty cash.
   d. U.S. Treasury bills.

135. Which of the following would not be reported on the balance sheet as a cash equivalent?
   a. Money market fund
   b. Sixty-day certificate of deposit
   c. Six-month Treasury bill
   d. Money market savings certificate

136. Compensating balances are a restriction on the use of a company's cash and should be
   a. reported as a current asset.
   b. reported as a noncurrent asset.
   c. disclosed in the financial statements.
   d. reported as a reduction of cash.

Additional Multiple Choice Questions

137. The principles of internal control include all of the following except
   a. establishment of responsibility.
   b. combining of duties.
   c. physical, mechanical, and electronic controls.
   d. independent internal verification.
138. An example of poor internal control is
   a. The accountant should not have physical custody of the asset nor access to it.
   b. The custodian of an asset should not maintain or have access to the accounting
      records.
   c. One person should be responsible for handling related transactions.
   d. A salesperson makes the sale, and a different person ships the goods.

139. Having different individuals receive cash, record cash receipts, and hold the cash is an
     example of
     a. establishment of responsibility.
     b. segregation of duties.
     c. documentation procedures.
     d. independent internal verification.

140. Storing cash in a company safe is an application of which internal control principle?
     a. Segregation of duties
     b. Documentation procedures
     c. Physical controls
     d. Establishment of responsibility

141. Using prenumbered checks and having an approved invoice for each check is an example
     of
     a. establishment of responsibility.
     b. segregation of duties.
     c. documentation procedures.
     d. independent internal verification.

142. An application of good internal control over cash disbursements is
     a. following payment, the approved invoice should be stamped PAID.
     b. blank checks should be stored in the treasurer's desk.
     c. each check should be compared with the approved invoice after the check is issued.
     d. check signers should record the cash disbursements.

143. When making a payment from the petty cash fund for postage stamps, the following
     journal entry is made.
     a. Office Supplies ......................... XXXX
        Petty Cash ........................  XXXX
     b. Postage Expense ..................... XXXX
        Petty Cash ........................  XXXX
     c. Miscellaneous Expense............ XXXX
        Petty Cash ........................  XXXX
     d. No entry is made.

144. All of the following would involve a debit memorandum except
     a. a bank service charge.
     b. an NSF check.
     c. the cost of printing checks.
     d. interest earned.
145. A bank may issue a credit memorandum for
   a. a bank service charge.
   b. an NSF (not sufficient funds) check from a customer.
   c. the collection of a note receivable for the depositor by the bank.
   d. the cost of printing checks.

146. Journal entries are required by the depositor for all of the following except
   a. collection of a note receivable.
   b. bank errors.
   c. bank service charges.
   d. an NSF check.

147. Cash equivalents are highly liquid investments that can be converted into a specific
     amount of cash with maturities of
   a. 1 month or less when purchased.
   b. 3 months or less when purchased.
   c. 6 months or less when purchased.
   d. 1 year or less when purchased.

---

**Answers to Multiple Choice Questions**

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BRIEF EXERCISES

BE 148

Match the principle of internal control to each of the following cases.

a) Establishment of responsibility
b) Segregation of duties
c) Accountability for assets
d) Documentation procedures
e) Physical, mechanical and electronic controls

_____ 1. Employees’ time is tracked using a time clock.
_____ 2. Employees who receive shipments of goods do not have access to the accounting records for merchandise.
_____ 3. Shipping documents are prenumbered.
_____ 4. The bookkeeper does not have physical custody of assets.
_____ 5. Only the treasurer of the company can sign checks.

Solution 148 (4 min.)
1. e
2. b
3. d
4. b
5. a

BE 149

Identify which principle of internal control is being followed in each of the following cases.
1. Warehouse employees do not have access to the accounting records.
2. Prenumbered shipping documents are prepared for each shipment of goods.
3. The locked warehouse is accessible only by warehouse employees with keys.

Solution 149 (3 min.)
1. Segregation of duties
2. Documentation procedures
3. Physical controls
BE 150
Identify the internal control procedures applicable to cash receipts for Colorado Company in each of the following cases.
1. All cashiers are bonded.
2. The treasurer compares the total cash receipts to the bank deposit daily.
3. The bookkeeper records cash receipts which are held by the treasurer.
4. Only the treasurer holds cash receipts.
5. Deposit slips are completed for each deposit.

Solution 150 (4 min.)
1. Other controls
2. Independent internal verification
3. Segregation of duties
4. Establishment of responsibility
5. Documentation procedures.

BE 151
Identify the internal control procedures applicable to cash disbursements followed by Kerry Company in each of the following cases.
1. Company checks are prenumbered.
2. Only the treasurer is authorized to sign checks.
3. Invoices are stamped PAID.
4. Blank checks are stored in a locked safe.
5. The bookkeeper, not the treasurer, records cash disbursements.

Solution 151 (4 min.)
1. Documentation procedures
2. Establishment of responsibility
3. Other controls
4. Physical controls
5. Segregation of duties

BE 152
On October 1, Grayson Company’s petty cash fund of $120 is replenished. The fund contains cash of $40, and receipts for supplies of $55 and postage of $25. Prepare the journal entry to record the replenishment of the petty cash fund.

Solution 152 (3 min.)
Supplies ................................................................. 55
Postage Expense .................................................... 25
Cash ................................................................. 80
BE 153
Identify whether each of the following items would be (a) added to the book balance, or (b) deducted from the book balance in a bank reconciliation.
1. EFT transfer to a supplier
2. Bank service charge
3. Check printing charge
4. Error recording check # 214 which was written for $230 but recorded for $320
5. Collection of note and interest by bank on company’s behalf

Solution 153 (3 min.)
1. b
2. b
3. b
4. a
5. a

BE 154
Identify whether each of the following items would be (a) added to the book balance, (b) deducted from the book balance in a bank reconciliation, (c) added to the bank balance, or (d) deducted from the bank balance.
1. Deposits in transit
2. Bank service charge
3. Collection of note and interest by bank on company’s behalf
4. NSF check
5. Outstanding checks

Solution 154 (4 min.)
1. c
2. b
3. a
4. b
5. d

BE 155
Identify which of the following reconciling items would require an adjusting entry to be made by Beutron Company.
1. Deposits in transit totaled $2,000.
2. A check written to the company for $350 by Taxton Company was returned NSF.
3. The bank charged the company $46 for printing checks.
4. Outstanding checks totaled $1,667
5. A debit memorandum reported an EFT of $178 to Paco Utilities
Solution 155  (3 min.)
Adjusting entries would be required for: 2, 3, and 5 because they are reconciling items for the books.

BE 156
Acton Company needs to make adjusting entries for each of the following reconciling items. Identify the account to be debited and the account to be credited in each case.
1. A check for $59 written to the company by J. Neutron was returned NSF.
2. The monthly service charge by the bank was $34.
3. The bank collected a $1,000 note plus interest of $97 on the company’s behalf. The company had not accrued the interest.

Solution 156  (4 min.)
1. Debit: Accounts Receivable  Credit: Cash
2. Debit: Miscellaneous Expense  Credit: Cash
3. Debit: Cash  Credit: Note Receivable, Interest Revenue

BE 157
The following reconciling items are applicable to the bank reconciliation for the Motley Crew Company. Indicate how each item should be shown on a bank reconciliation.

a. Outstanding checks.
b. Bank credit memorandum for collecting a note for the depositor.
c. Bank debit memorandum for service charge.
d. Deposit in transit.

Solution 157  (4 min.)
a. Outstanding checks should be deducted from the balance per bank.
b. Bank credit memorandum should be added to the balance per books.
c. Bank debit memorandum should be deducted from the balance per books.
d. Deposits in transit should be added to the balance per bank.

BE 158
At August 31, Jones Company has this bank information: cash balance per bank $6,950; outstanding checks $762; deposits in transit $1,700; and a bank service charge $20. Determine the adjusted cash balance per bank at August 31, 2008.
Solution 158  (5 min.)

Jones Company
Partial Bank Reconciliation
August 31, 2008

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
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<tbody>
<tr>
<td>Cash balance per bank</td>
<td>$6,950</td>
</tr>
<tr>
<td>Add: Deposit in transit</td>
<td>1,700</td>
</tr>
<tr>
<td>Less: Outstanding checks</td>
<td>762</td>
</tr>
<tr>
<td>Adjusted cash balance per bank</td>
<td>$7,888</td>
</tr>
</tbody>
</table>

BE 159

Given the following information, determine the adjusted cash balance per books from the following information:

a. Balance per books as of June 30, $9,300.
b. Outstanding checks, $600.
c. NSF check returned with bank statement, $130.
d. Deposit mailed the afternoon of June 30, $300.
e. Check printing charges, $30.
f. Interest earned on checking account, $40.

Solution 159  (4 min.)

$9,180: ($9,300 – $130 – $30 + $40)

EXERCISES

Ex. 160

Match each of the following principles of internal control with the appropriate description below.

A. Establishment of responsibility
B. Segregation of duties
C. Documentation procedures
D. Physical, mechanical, and electronic controls
E. Independent internal verification
F. Other controls

_____ 1. Involves the review, comparison, and reconciliation of data prepared by other employees.
_____ 2. Provide evidence that transactions and events have occurred.
_____ 3. Includes the authorization and approval of transactions.
_____ 4. Rotating employees' duties and requiring employees to take vacations.
_____ 5. Related activities should be assigned to different individuals.
_____ 6. Using garment sensors to deter theft.
Solution 160  (5 min.)
1. E  3. A  5. B

Ex. 161
Below are descriptions of internal control problems. In the space to the left of each item, enter the code letter of the one best internal control principle that relates to the problem described.

<table>
<thead>
<tr>
<th>Internal Control Principles</th>
<th>Code Letter</th>
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<tbody>
<tr>
<td>A. Establishment of responsibility</td>
<td>B</td>
</tr>
<tr>
<td>B. Segregation of duties</td>
<td>D</td>
</tr>
<tr>
<td>C. Physical, mechanical, and electronic control devices</td>
<td>E</td>
</tr>
<tr>
<td>D. Documentation procedures</td>
<td>F</td>
</tr>
<tr>
<td>E. Independent internal verification</td>
<td></td>
</tr>
<tr>
<td>F. Other controls</td>
<td></td>
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</tbody>
</table>

   1. The same person opens incoming mail and posts the accounts receivable subsidiary ledger.
   2. Three people handle cash sales from the same cash register drawer.
   3. A clothing store is experiencing a high level of inventory shortages because people try on clothing and walk out of the store without paying for the merchandise.
   4. The person who is authorized to sign checks approves purchase orders for payment.
   5. Some cash payments are not recorded because checks are not prenumbered.
   6. Cash shortages are not discovered because there are no daily cash counts by supervisors.
   7. The treasurer of the company has not taken a vacation for over 20 years.

Solution 161  (5 min.)
1. B  5. D
3. C  7. F
4. B

Ex. 162
Dan Howe has worked for Dr. Pat Dorsey for several years. Dan demonstrates a loyalty that is rare among employees. He hasn't taken a vacation in the last three years. One of Dan's primary duties at the medical office is to open the mail and list the checks received. He also takes cash from patients at the cashier window as patients leave. At times it is so hectic that Dan doesn't bother with giving each patient a receipt for the cash paid on their accounts. He assures them he will see to it that they receive the proper credit. When the traffic is slow in the office, Dan offers to help Eve post the payments to the patients' accounts receivable. She is always happy to receive his help, because he is a very conscientious worker.

Instructions
Identify any principles of internal control that may be violated in this medical office situation.
Solution 162  (10 min.)

Violations:

1. It is Eve's responsibility to post payments to patient accounts. In allowing Dan to assist her, the establishment of responsibility principle is violated.

2. Although it appears to be a small office, it is not appropriate that Dan both opens the mail, receives and records cash receipts from patients, and also appears to have custody of cash. This situation violates the segregation of duties principle. By posting to patients' accounts, it would be possible to post credits to patient accounts and pocket the cash.

3. The documentation principle is violated when patients are not given cash receipts. Although many professional offices do not have cash registers, computerized or manual receipts are customary and necessary.

4. Independent internal verification is also being violated. There is no independent counting of the cash and comparison to total receipts.

5. Other controls are being violated. There is no mention of Dan being bonded. Also, personnel should be required to take vacations.

Ex. 163

Listed below are seven errors or problems which might occur in the processing of cash transactions. Also shown is a list of internal control principles. Evaluate each possible error and cite a principle that is listed that would reduce the probability of the error occurring. If none of the principles given will correct the problem, write "None." If you think more than one principle is appropriate, list all principles that apply.

Possible Errors or Problems

1. An employee steals the cash collected from a customer for an account receivable and conceals this theft by issuing a credit memorandum indicating that the customer returned the merchandise.

2. A small fire destroys 3 days of cash receipts.

3. The official designated to sign checks is able to steal blank checks and issue them without fear of detection.

4. A salesclerk in serving customers often rings up a sale for less than the actual amount and then keeps the additional cash collected from the customer.

5. Three cashiers use one cash register drawer and the cash in the drawer is often short of the balance kept on hand.

6. Each cashier counts his own register drawer each day and verbally reports the results to the supervisor.

7. Cashiers with over 5 years’ experience are not bonded.

Internal Control Principles

a. Establishment of responsibility
b. Segregation of duties
c. Physical, mechanical, and electronic control devices
d. Documentation procedures
e. Independent internal verification
f. Other controls
Solution 163 (10 min.)
1. b 5. a and e
2. f and c 6. d and e
3. c 7. f
4. c

Ex. 164
Match the internal control principle below with the appropriate cash receipts procedure described.

a. Documentation procedures
b. Establishment of responsibility
c. Independent internal verification
d. Other controls
e. Physical, mechanical, and electronic controls
f. Segregation of duties

_____ 1. Only designated personnel are authorized to handle cash receipts.
_____ 2. Different individuals receive cash and record cash receipts.
_____ 3. Use remittance advice and cash register tapes.
_____ 4. Store cash in safes and bank vaults.
_____ 5. Treasurer compares total receipts to bank deposits daily.
_____ 6. Deposit all cash in bank daily.

Solution 164 (5 min.)
1. b 3. a 5. c
2. f 4. e 6. d

Ex. 165
Match the internal control principle below with the appropriate cash disbursements procedure described.

a. Establishment of responsibility
b. Segregation of duties
c. Documentation procedures
d. Physical, mechanical, and electronic controls
e. Independent internal verification
f. Other controls

_____ 1. Compare checks to invoices.
_____ 2. Different individuals approve and make payments.
_____ 3. Print check amounts by machine with indelible ink.
_____ 4. Only designated personnel are authorized to sign checks.
_____ 5. Each check must have approved invoice.
_____ 6. Stamp invoices PAID.
Solution 165 (5 min.)

1. e 3. d 5. c
2. b 4. a 6. f

Ex. 166

The petty cash fund of $200 for Walsh Company appeared as follows on December 31, 2008:

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<tr>
<th>Description</th>
<th>Amount</th>
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<tr>
<td>Cash</td>
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<td>Petty cash vouchers</td>
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<td>Freight in</td>
<td>$21.40</td>
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<tr>
<td>Postage</td>
<td>40.00</td>
</tr>
<tr>
<td>Balloons for a special occasion</td>
<td>18.00</td>
</tr>
<tr>
<td>Meals</td>
<td>25.00</td>
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</tbody>
</table>

Instructions

1. Briefly describe when the petty cash fund should be replenished. Because there is cash on hand, is there a need to replenish the fund at year end on December 31? Explain.

2. Prepare in general journal form the entry to replenish the fund.

3. On December 31, the office manager gives instructions to increase the petty cash fund by $100. Make the appropriate journal entry.

Solution 166 (10 min.)

1. Petty cash should be replenished on a periodic basis or when the cash is low. It must be replenished on the balance sheet date so that the expenses represented by the petty cash vouchers can be recorded in the proper accounting period.

2. Freight-in.......................................................................................... 21.40
   Postage Expense............................................................................. 40.00
   Miscellaneous Expense................................................................... 18.00
   Meals Expense................................................................................. 25.00
   Cash Over and Short ....................................................................... 2.00
   Cash........................................................................................ 106.40

3. Petty Cash........................................................................................ 100.00
   Cash........................................................................................ 100.00

Ex. 167

Prepare the entry to replenish the $200 petty cash fund of Warner Company, assuming the fund has receipts for: freight-out $60, postage $105, and miscellaneous expense $20. The fund contains $10 in cash.
Solution 167  (5 min.)

Freight-out .............................................................................................................  60
Postage Expense .................................................................................................  105
Miscellaneous Expense ..................................................................................  20
Cash Over and Short ......................................................................................  5
Cash ($200 – $10) ............................................................................................... 190

Ex. 168

On October 1, 2008, Foster Company establishes an imprest petty cash fund by issuing a check for $200 to Mary Mann, the custodian of the petty cash fund. On October 31, 2008, Mary Mann submitted the following paid petty cash receipts for replenishment of the petty cash fund when there is $55 cash in the fund:

Freight-in $27
Office Supplies Expense 35
Entertainment of Clients 60
Postage Expense 20

Instructions

Prepare the journal entries required to establish the petty cash fund on October 1 and the replenishment of the fund on October 31.

Solution 168  (10 min.)

Oct.  1 Petty Cash...........................................................................  200
     Cash ...........................................................................  200
     (To establish a petty cash fund)

   31 Cash Over and Short...........................................................  3
     Freight-in..............................................................................  27
     Office Supplies Expense......................................................  35
     Entertainment Expense .......................................................  60
     Postage Expense.................................................................  20
     Cash ...........................................................................  145
     (To record expenses for October and to replenish
      the petty cash fund)

Ex. 169

Ogleby Boat Company's bank statement for the month of September showed a balance per bank of $7,000. The company's Cash account in the general ledger had a balance of $5,459 at September 30. Other information is as follows:

(1) Cash receipts for September 30 recorded on the company's books were $5,700 but this amount does not appear on the bank statement.

(2) The bank statement shows a debit memorandum for $40 for check printing charges.
Ex. 169  (cont.)

(3) Check No. 119 payable to Lann Company was recorded in the cash payments journal and cleared the bank for $248. A review of the accounts payable subsidiary ledger shows a $36 credit balance in the account of Lann Company and that the payment to them should have been $284.

(4) The total amount of checks still outstanding at September 30 amounted to $6,000.

(5) Check No. 138 was correctly written and paid by the bank for $409. The cash payment journal reflects an entry for Check No. 138 as a debit to Accounts Payable and a credit to Cash in Bank for $490.

(6) The bank returned an NSF check from a customer for $360.

(7) The bank included a credit memorandum for $1,560 which represents collection of a customer's note by the bank for the company; principal amount of the note was $1,500 and interest was $60. Interest has not been accrued.

Instructions
(a) Prepare a bank reconciliation for Ogleby Boat Company at September 30.
(b) Prepare any adjusting entries necessary as a result of the bank reconciliation.

Solution 169  (25 min.)

(a) OGLEBY BOAT COMPANY
Bank Reconciliation
September 30

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash balance per bank</td>
<td>$7,000</td>
</tr>
<tr>
<td>Add:</td>
<td></td>
</tr>
<tr>
<td>(1) Deposit in transit</td>
<td>$5,700</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
</tr>
<tr>
<td>(4) Outstanding checks</td>
<td>$6,000</td>
</tr>
<tr>
<td>Adjusted cash balance per books</td>
<td>$6,700</td>
</tr>
</tbody>
</table>

Cash balance per books $5,459

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Add:</td>
<td></td>
</tr>
<tr>
<td>(5) Accounts Payable Error</td>
<td>$81</td>
</tr>
<tr>
<td>(7) Collect $1,500 note and interest $60</td>
<td>$1,560</td>
</tr>
<tr>
<td></td>
<td>$1,641</td>
</tr>
<tr>
<td></td>
<td>$7,100</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
</tr>
<tr>
<td>(2) Check printing</td>
<td>$40</td>
</tr>
<tr>
<td>(6) NSF Check</td>
<td>$360</td>
</tr>
<tr>
<td></td>
<td>$400</td>
</tr>
<tr>
<td>Adjusted cash balance per books</td>
<td>$6,700</td>
</tr>
</tbody>
</table>

Note: Item (3) is not a reconciling item.

(b)

Sept. 30  Cash ................................................................. 81
          Accounts Payable ........................................ 81
          (To correct error in recording Check No. 138)

30  Cash ................................................................. 1,560
    Notes Receivable ........................................ 1,500
    Interest Revenue ........................................ 60
    (To record collection of note receivable and interest by the bank)
30 Miscellaneous Expense ....................................................  40
Cash.........................................................................   40
(To record check printing charges)

30 Accounts Receivable ........................................................  360
Cash.........................................................................   360
(To record NSF check)

Ex. 170
Reebles Food Store developed the following information in recording its bank statement for the month of March.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance per books March 31</td>
<td>$2,905</td>
</tr>
<tr>
<td>Balance per bank statement March 31</td>
<td>$10,900</td>
</tr>
</tbody>
</table>

(1) Checks written in March but still outstanding $7,000.
(2) Checks written in February but still outstanding $2,800.
(3) Deposits of March 30 and 31 not yet recorded by bank $5,200.
(4) NSF check of customer returned by bank $1,200.
(5) Check No. 210 for $594 was correctly issued and paid by bank but incorrectly entered in the cash payments journal as payment on account for $549.
(6) Bank service charge for March was $50.
(7) A payment on account was incorrectly entered in the cash payments journal and posted to the accounts payable subsidiary ledger for $824 when Check No. 318 was correctly prepared for $284. The check cleared the bank in March.
(8) The bank collected a note receivable for the company for $4,000 plus $150 interest revenue.

Instructions
Prepare a bank reconciliation at March 31.

Solution 170  (20 min.)

REEBLES FOOD STORE
Bank Reconciliation
March 31

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash balance per books</td>
<td>$2,905</td>
</tr>
<tr>
<td>Add:</td>
<td></td>
</tr>
<tr>
<td>(7) Error on Check No. 318</td>
<td>$ 540</td>
</tr>
<tr>
<td>(8) Collect $4,000 note and interest $150</td>
<td>4,150</td>
</tr>
<tr>
<td></td>
<td>7,595</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
</tr>
<tr>
<td>(4) NSF Check</td>
<td>1,200</td>
</tr>
<tr>
<td>(5) Error on Check No. 210</td>
<td>45</td>
</tr>
<tr>
<td>(6) Bank Service Charge</td>
<td>50</td>
</tr>
<tr>
<td></td>
<td>1,295</td>
</tr>
<tr>
<td>Adjusted cash balance per books</td>
<td>$6,300</td>
</tr>
<tr>
<td>Adjusted cash balance per bank</td>
<td>$ 6,300</td>
</tr>
</tbody>
</table>
Ex. 171

Using the code letters below, indicate how each of the items listed would be handled in preparing a bank reconciliation. Enter the appropriate code letter in the space to the left of each item.

Code
- A Add to cash balance per books
- B Deduct from cash balance per books
- C Add to cash balance per bank
- D Deduct from cash balance per bank
- E Does not affect the bank reconciliation

Items:
- ___ 1. Outstanding checks.
- ___ 2. Bank service charge.
- ___ 3. Check for $320 correctly written and paid by the bank but incorrectly entered in the cash payments journal for $230.
- ___ 4. Deposit in transit.
- ___ 5. Bank returns deposited check marked NSF.
- ___ 7. Bank debit memorandum for check printing fees.
- ___ 8. Petty cash custodian has $86 in paid petty cash vouchers that have not been reimbursed.
- ___ 9. Bank charged a check against the company which should have been charged to another company.
- ___ 10. A check for $236 was correctly paid by the bank but was incorrectly entered in the cash payments journal for $263.

Solution 171 (10 min.)

1. D 6. A
2. B 7. B
5. B 10. A
Ex. 172

The following adjusting entries for Rush Company were prepared after completing a bank reconciliation. For each of the following adjustments, prepare a probable explanation for the adjusting entry.

1. Supplies
   - Supplies on books: $150
   - Cash on books: $150
   - Explanation: To adjust book balance for error in recording supplies.

2. Accounts Receivable—B. Lowe
   - Accounts Receivable on books: $420
   - Cash on books: $420
   - Explanation: To record an NSF check returned with the bank statement.

3. Cash
   - Cash on books: $2,200
   - Notes Receivable on books: $2,000
   - Interest Revenue on books: $200
   - Explanation: To record collection of Notes Receivable and interest upon notification by bank through bank statement.

4. Sales
   - Sales on books: $81
   - Cash on books: $81
   - Explanation: To adjust book balance for transposition error in recording sales.

5. Miscellaneous Expense
   - Miscellaneous Expense on books: $20
   - Cash on books: $20
   - Explanation: To reduce the book balance for bank service or check printing charges.

Solution 172  (10 min.)

1. To adjust book balance for error in recording supplies.
2. To record an NSF check returned with the bank statement.
3. To record collection of Notes Receivable and interest upon notification by bank through bank statement.
4. To adjust book balance for transposition error in recording sales.
5. To reduce the book balance for bank service or check printing charges.

Ex. 173

The cash balance per books for Dexter Company on September 30, 2008 is $10,740.93. The following checks and receipts were recorded for the month of October, 2008:

<table>
<thead>
<tr>
<th>No.</th>
<th>Amount</th>
<th>No.</th>
<th>Amount</th>
<th>Amount</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>17</td>
<td>$372.96</td>
<td>22</td>
<td>$ 578.84</td>
<td>$843.86</td>
<td>10/  5</td>
</tr>
<tr>
<td>18</td>
<td>$780.62</td>
<td>23</td>
<td>$1,687.50</td>
<td>$941.54</td>
<td>10/21</td>
</tr>
<tr>
<td>19</td>
<td>$157.00</td>
<td>24</td>
<td>$ 921.30</td>
<td>$808.58</td>
<td>10/27</td>
</tr>
<tr>
<td>20</td>
<td>$587.50</td>
<td>25</td>
<td>$ 246.03</td>
<td>$967.00</td>
<td>10/30</td>
</tr>
<tr>
<td>21</td>
<td>$234.15</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Ex. 173  (cont.)

In addition, the bank statement for the month of October is presented below:

<table>
<thead>
<tr>
<th>Balance Last Statement</th>
<th>Deposits and Credits</th>
<th>Checks and Debits</th>
<th>Balance This Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>$5,404.84</td>
<td>5</td>
<td>10</td>
<td>$10,951.01</td>
</tr>
<tr>
<td>$9,178.36</td>
<td></td>
<td>$3,632.19</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Checks and other debits</th>
<th>Deposits</th>
<th>Date</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>No.</td>
<td>Amount</td>
<td>No.</td>
<td>Amount</td>
</tr>
<tr>
<td>14</td>
<td>148.29</td>
<td>17</td>
<td>372.96</td>
</tr>
<tr>
<td>18</td>
<td>708.62</td>
<td>24</td>
<td>921.30</td>
</tr>
<tr>
<td>19</td>
<td>157.00</td>
<td>25</td>
<td>246.03</td>
</tr>
<tr>
<td>21</td>
<td>234.15</td>
<td></td>
<td>25.00</td>
</tr>
<tr>
<td></td>
<td>240.00</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Symbols: NSF (Not sufficient funds)  SC (Service charge)  CM (Credit Memo)

Check No. 18 was correctly written for $708.62 for a payment on account. The NSF check was from S. King, a customer, in settlement of an accounts receivable. An entry had not been made for the NSF check. The credit memo is for the collection of a note receivable including interest of $60 which has not been accrued. The bank service charge is $25.00.

Instructions
(a) Prepare a bank reconciliation at October 31.
(b) Prepare the adjusting journal entries required by the bank reconciliation.

Solution 173  (30–35 min.)

(a) DEXTER COMPANY
Bank Reconciliation
October 31, 2008

Cash balance per bank statement .............................................. $10,951.01
Add: Deposits in transit .......................................................... 967.00
-----------------------------------------------
$11,918.01

Less: Outstanding checks
No. 20 ........................................................................ $ 587.50
No. 23 ........................................................................ 1,687.50  2,275.00

Adjusted cash balance per bank ................................................ $ 9,643.01

Cash balance per books .......................................................... $ 8,736.01*
Add: Error in recording check No. 18 ........................................ $  72.00
Note collected by bank ............................................................ 1,100.00  1,172.00
-----------------------------------------------
9,908.01

Less: Bank service charge ......................................................... 25.00
NSF check .................................................................. 240.00  265.00

Adjusted cash balance per books .............................................. $ 9,643.01

*9/30 balance per books + Receipts – Checks written = 10/31 balance per books
$10,740.93 + $3,560.98 – $5,565.90 = $8,736.01
Solution 173  (cont.)

(b) Oct. 31  
Cash .......................... 72.00
Accounts Payable .......................... 72.00
(To correct recording error on check No. 18)

31  
Cash ........................................... 1,100.00
Notes Receivable .......................... 1,040.00
Interest Revenue .......................... 60.00
(To record collection of note and interest)

31  
Miscellaneous Expense .......................... 25.00
Cash ........................................... 25.00
(To record bank service charge for the month of October)

31  
Accounts Receivable—S. King .......................... 240.00
Cash ........................................... 240.00
(To record NSF check)

Ex. 174
Simon Company received a notice with its bank statement that the bank had collected a note receivable for $6,000 plus $300 of interest. The bank had credited these amounts to Simon's account less a collection fee of $10. Simon Company had already accrued the interest for this note on its books.

(a) How will these items affect Simon Company's bank reconciliation?

(b) Prepare the journal entry that Simon Company will make to record this information on its books.

Solution 174  (5 min.)

(a) Simon Company must add the amount of the note plus interest less the collection charge to its cash balance per books on the bank reconciliation.

Add:  Collection of note receivable $6,290

(b)  
Cash ........................................... 6,290
Miscellaneous Expense .......................... 10
Note Receivable .......................... 6,000
Interest Receivable .......................... 300
Ex. 175

The cash records of Norris Company show the following:

1. The June 30 bank reconciliation indicated that deposits in transit totaled $390. During July the general ledger account Cash shows deposits of $9,800, but the bank statement indicates that only $9,240 in deposits were received during the month.

2. The June 30 bank reconciliation also reported outstanding checks of $800. During the month of July, Norris Company books show that $11,070 of checks were issued, yet the bank statement showed that $11,100 of checks cleared the bank in July.

There were no bank debit or credit memoranda and no errors were made by either the bank or Norris Company.

Answer the following questions:
(a) What were the deposits in transit at July 31?
(b) What were the outstanding checks at July 31?

Solution 175  (10 min.)

(a) Deposits in Transit:
   
   Deposits per books in July .............................................   $  9,800
   Deposits per the bank in July .........................................  $  9,240
   Less: June 30 deposits in transit....................................         390
   July receipts deposited in July .......................................       8,850
   Deposits in transit, July 31 .............................................   $     950

(b) Outstanding Checks:
   
   Checks per books in July ...............................................   $11,070
   Checks clearing the bank in July....................................  $11,100
   Less: Outstanding checks, June 30 ..............................         800
   July checks clearing in July............................................     10,300
   Outstanding checks, July 31 ..........................................   $     770

Ex. 176

Indicate how each of the following items would be shown on a bank reconciliation.

1. Bank error (The bank charged our account with another company's check)
2. Check printing charge
3. Deposits in transit
4. Note collected by the bank
5. NSF checks
6. Outstanding checks
Solution 176  (7 min.)
1. Added to balance per bank
2. Deducted from balance per books
3. Added to balance per bank
4. Added to balance per books
5. Deducted from balance per books
6. Deducted from balance per bank

Ex. 177
The cash records of Pine Company show the following:

1. In September, deposits per the bank statement totaled $37,600; deposits per books $39,000; and deposits in transit at September 30 were $4,300.
2. In September, cash disbursements per books were $36,500; checks clearing the bank were $37,800; and outstanding checks at September 30 were $2,500.

There were no bank debit or credit memoranda and no errors were made by either the bank or Pine Company.

Answer the following questions:
(a) What were the deposits in transit at August 31?
(b) What were the outstanding checks at August 31?

Solution 177  (10 min.)
(a) Deposits in Transit:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deposits per bank statement in September</td>
<td>$37,600</td>
</tr>
<tr>
<td>Add: Deposits in transit, September 30</td>
<td>4,300</td>
</tr>
<tr>
<td>Total deposits to be accounted for</td>
<td>41,900</td>
</tr>
<tr>
<td>Less: Deposits per books</td>
<td>39,000</td>
</tr>
<tr>
<td>Deposits in transit, August 31</td>
<td>$ 2,900</td>
</tr>
</tbody>
</table>

(b) Outstanding Checks:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Checks clearing the bank in September</td>
<td>$37,800</td>
</tr>
<tr>
<td>Add: Outstanding checks, September 30</td>
<td>2,500</td>
</tr>
<tr>
<td>Total checks to be accounted for</td>
<td>40,300</td>
</tr>
<tr>
<td>Less: Cash disbursements per books</td>
<td>36,500</td>
</tr>
<tr>
<td>Outstanding checks, August 31</td>
<td>$ 3,800</td>
</tr>
</tbody>
</table>
Ex. 178

Listed below are items that may be useful in preparing the March 2008, bank reconciliation for Korman Machine Works.

Using the following code, insert in the space before each item the letter where the amount would be located or otherwise treated in the bank reconciliation process.

<table>
<thead>
<tr>
<th>Code</th>
<th>Located or Treated</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Add to the cash balance per books</td>
</tr>
<tr>
<td>B</td>
<td>Deduct from the cash balance per books</td>
</tr>
<tr>
<td>C</td>
<td>Add to the cash balance per bank</td>
</tr>
<tr>
<td>D</td>
<td>Deduct from the cash balance per bank</td>
</tr>
<tr>
<td>E</td>
<td>Does not affect the bank reconciliation</td>
</tr>
</tbody>
</table>

_____ 1. Included with the bank statement materials was a check from Joe Terrell for $40 stamped "account closed."

_____ 2. A personal deposit by Tim Korman to his personal account in the amount of $300 for dividends on his General Electric common stock was credited to the company account.

_____ 3. The bank statement included a debit memorandum for $22.00 for two books of blank checks for Korman Machine Works.

_____ 4. The bank statement contains a credit memorandum for $24.75 interest on the average checking account balance.

_____ 5. The daily deposits of March 30 and March 31, for $3,362 and $3,125 respectively, were not included in the bank statement postings.

_____ 6. Two checks totaling $316.86, which were outstanding at the end of February, cleared in March and were returned with the March statement.

_____ 7. The bank statement included a credit memorandum dated March 28, 2008, for $45.00 for the monthly interest on a 6-month, $15,000 certificate of deposit that the company owns.

_____ 8. Four checks, #8712, #8716, #8718, #8719, totaling $5,369.65, did not clear the bank during March.


_____ 10. The bank statement included a debit memorandum for $25.00 for the collection service on the above note and interest.

Solution 178  (10 min.)

1. B
2. D
3. B
4. A
5. C
6. E
7. A
8. D
9. A
10. B
Ex. 179

The following information was used to prepare the March 2008, bank reconciliation for Korman Machine Works. Identify the items that require adjustment to the cash balance per books and prepare the appropriate adjusting entries.

1. Included with the bank statement materials was a check from Joe Terrell for $40 stamped "NSF."

2. A personal deposit by Tim Korman to his personal account in the amount of $300 for dividends on his General Electric common stock was credited to the company account.

3. The bank statement included a debit memorandum for $22.00 for two books of blank checks for Korman Machine Works.

4. The bank statement contains a credit memorandum for $24.75 interest on the average checking account balance.

5. The daily deposits of March 30 and March 31, for $3,362 and $3,125 respectively, were not included in the bank statement postings.

6. Two checks totaling $316.86, which were outstanding at the end of February, cleared in March and were returned with the March statement.

7. The bank statement included a credit memorandum dated March 28, 2008, for $45.00 for the monthly interest on a 6-month, $15,000 certificate of deposit that the company owns.

8. Four checks, #8712, #8716, #8718, #8719, totaling $5,369.65, did not clear the bank during March.


10. The bank statement included a debit memorandum for $25.00 for the collection service on the above note and interest.

Solution 179  (20 min.)

<table>
<thead>
<tr>
<th>Item #</th>
<th>Description</th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>#1</td>
<td>Accounts Receivable</td>
<td></td>
<td>40.00</td>
</tr>
<tr>
<td></td>
<td>Cash</td>
<td></td>
<td>40.00</td>
</tr>
<tr>
<td>#3</td>
<td>Miscellaneous Expense</td>
<td></td>
<td>22.00</td>
</tr>
<tr>
<td></td>
<td>Cash</td>
<td></td>
<td>22.00</td>
</tr>
<tr>
<td>#4</td>
<td>Cash</td>
<td></td>
<td>24.75</td>
</tr>
<tr>
<td></td>
<td>Interest Revenue</td>
<td></td>
<td>24.75</td>
</tr>
<tr>
<td>#7</td>
<td>Cash</td>
<td></td>
<td>45.00</td>
</tr>
<tr>
<td></td>
<td>Interest Revenue</td>
<td></td>
<td>45.00</td>
</tr>
<tr>
<td>#9</td>
<td>Cash</td>
<td></td>
<td>4,590</td>
</tr>
<tr>
<td></td>
<td>Note Receivable</td>
<td></td>
<td>4,500</td>
</tr>
<tr>
<td></td>
<td>Interest Revenue</td>
<td></td>
<td>90</td>
</tr>
<tr>
<td>#10</td>
<td>Miscellaneous Expense</td>
<td></td>
<td>25.00</td>
</tr>
<tr>
<td></td>
<td>Cash</td>
<td></td>
<td>25.00</td>
</tr>
</tbody>
</table>
Ex. 180
Compute Nance Company’s adjusted cash balance per books based on the following information:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning cash balance per books</td>
<td>$4,500</td>
</tr>
<tr>
<td>Deposit in transit</td>
<td>800</td>
</tr>
<tr>
<td>Check printing charge</td>
<td>20</td>
</tr>
<tr>
<td>Note collected by bank for Nance</td>
<td>1,500</td>
</tr>
</tbody>
</table>

Solution 180  (5 min.)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning cash balance per books</td>
<td>$4,500</td>
</tr>
<tr>
<td>Add: Collection of note</td>
<td>1,500</td>
</tr>
<tr>
<td></td>
<td>6,000</td>
</tr>
<tr>
<td>Less: Check printing charge</td>
<td>20</td>
</tr>
<tr>
<td>Adjusted cash balance per books</td>
<td>$5,980</td>
</tr>
</tbody>
</table>
COMPLETION STATEMENTS

181. Internal control consists of the related methods and measures adopted to __________ its assets and enhance the _____________ and _____________ of its accounting records.

182. The principle of internal control that prevents one individual from being responsible for all the related activities of a given task is _____________.

183. Maintaining an adequate system of internal control is required by the ______________ Act of 1977.

184. The _____________ of an asset should not have access to the accounting records of that asset.

185. Employees of a company who evaluate the effectiveness of the company's system of internal controls on a year-round basis are called _____________.

186. Using _____________ documents is a control measure which helps in accounting for all documents in a series and also prevents a document from being recorded more than once.

187. Employees who handle cash should be _____________ in order to protect against misappropriation of assets by dishonest employees.

188. Two limitations of systems of internal control are the concept of _____________ and the _____________.

189. Internal control over cash disbursements is more effective when payments are made by _____________, rather than by _____________.

190. A disbursement system that uses wire, telephone, computers, etc., to transfer cash from one location to another is referred to as _______________.

191. A voucher is recorded in the _____________ and filed according to the date on which it is to be paid.

192. A ________________ fund is used to pay relatively small expenditures.

193. A debit memorandum issued by the bank ______________ the cash balance in the depositor's account.

194. There are three parties to a check: (1)_______________, (2)_______________, and the (3)_______________.
195. The difference between the cash in bank balance shown on the company's books and the cash balance shown on the bank statement may be caused by ______________ and by ______________ in recording transactions by either party.

196. In preparing a bank reconciliation, outstanding checks are ______________ from the cash balance per ______________.

197. A check correctly written for $270 was incorrectly entered in the cash payments journal for $720. In preparing a bank reconciliation, $_____________ must be ______________ the cash balance per ______________.

Answers to Completion Statements

181. safeguard, accuracy, reliability
182. segregation of duties
183. Foreign Corrupt Practices
184. custodian
185. internal auditors
186. prenumbered
187. bonded
188. reasonable assurance, human element
189. check, cash
190. electronic funds transfer (EFT)
191. voucher register
192. petty cash
193. reduces
194. maker, payer, payee
195. time lags, errors
196. deducted, bank
197. $450, added to, books
MATCHING

198. Match the items below by entering the appropriate code letter in the space provided.

A. Prenumbered documents
B. Custody of an asset should be kept separate from the record-keeping for that asset
C. Cash registers, garment sensors and burglar alarms are examples
D. Bonding employees
E. Collusion
F. Cash
G. Bank signature card
H. Payee
I. Maker
J. Canceled checks
K. NSF checks
L. Outstanding checks
M. Petty cash receipt
N. Cash equivalents
O. Voucher system

____  1. Segregation of duties.
____  2. One to whom a check is payable.
____  3. Two or more employees circumventing prescribed procedures.
____  4. Prevent a transaction from being recorded more than once.
____  5. Checks which have been returned by the maker's bank for lack of funds.
____  6. Checks which have been paid by the depositor's bank.
____  7. Indicates those people authorized to sign checks.
____  8. Anything that a bank will accept for deposit.
____ 10. One who issues a check.
____ 11. Insurance protection against misappropriation of assets.
____ 12. An extensive network of approvals by authorized individuals.
____ 14. Issued checks that have not been paid by the bank.
____ 15. Highly liquid investments.

Answers to Matching

5. K  10. I  15. N
SHORT-ANSWER ESSAY QUESTIONS

S-A E 199

Important objectives of a system of internal controls are to safeguard assets and to enhance the accuracy and reliability of the accounting records. Briefly discuss how (1) cost-benefit considerations, (2) the human element, and (3) the size of the business, affect the implementation of a system of internal controls.

Solution 199

The implementation of a system of internal controls is affected by cost benefit considerations, the human element, and the size of the business. A company's system of internal control can provide reasonable assurance, but not absolute assurance, that assets are properly safeguarded and that the accounting records are reliable. The concept of reasonable assurance rests on the premise that the costs of establishing control procedures should not exceed their expected benefit. A very costly set of safeguards may produce something approaching absolute assurance, but the value of the benefits received would not come close to outweighing the costs.

The human element can cause a good system of internal control to become ineffective due to employee fatigue, carelessness, or indifference. Additionally, collusion between two or more employees to circumvent prescribed controls may significantly impair the effectiveness of the system.

The size of a business impacts internal control because a smaller business may not have the necessary resources available to affect the implementation of desirable controls.

S-A E 200

Your friend, Mark, has opened a movie theater. Mark states that he does not have time to develop and implement a system of internal controls.

a. Provide Mark with the objectives of a system of internal controls.

b. Explain to Mark why he should develop a system of internal controls.

Solution 200

a. The objectives of a system of internal controls include:
   1. safeguarding assets from employee theft, robbery, and unauthorized use
   2. enhancing the accuracy and reliability of its accounting records by reducing the risk of errors and irregularities in the accounting process.

b. Mark, here are some reasons why you must develop a system of internal controls:
   1. You will not be able to oversee every function of your business. For this reason, you must establish policies and procedures for your employees to follow. By designing these policies and procedures around the principles of internal control, you have a foundation for safeguarding assets and enhancing the accuracy and reliability of the accounting records.
   2. A good system of internal controls will help you attract investors and creditors because they will value the rewards of the system.
   3. A good system of internal controls works to eliminate fraud. No business can assume that fraud will not take place.
S-A E 201
The preparation of a bank reconciliation is an important cash control procedure. If a company deposits cash receipts daily and makes all cash disbursements by check, explain why the cash balance per books might not agree with the cash balance shown on the bank statement. Identify specific examples that may cause differences between the cash balance per books and the cash balance per bank.

Solution 201
The cash balance per books will not agree with the cash balance shown on the bank statement due to time lags and errors by either party. A time lag could mean the bank records a transaction in a period later than the company records it (outstanding checks, deposits-in-transit) or the company records a transaction in a period later than the bank records it (NSF check, collection of a note, etc.). A common error is transposition of amounts in the recording process.

S-A E 202 (Ethics)
Tyler Instruments is a rapidly growing manufacturer of medical devices. As a result of its growth, the company's management recently modified several of its procedures and practices to improve internal control. Some employees are upset with the changes. They have complained that all these changes just show that the company no longer trusts them.

Required:
"Internal controls exist because most people can't be trusted." Is this true? Explain.

Solution 202
Internal controls exist, not because most people can't be trusted, but to protect the company's assets from those few who can't be trusted. If it were a perfect world, and everyone could be trusted, internal controls would not be needed. However, it does not follow that internal controls indicate the opposite.

It is true that anyone is capable of practically any action, if motivation and opportunity are both present. Since it is extremely difficult to measure motivation to directly or indirectly harm the company, let alone to monitor changes in motivation, a company's best recourse is to prevent opportunity.

Rather than feel threatened by internal control measures, honest employees should feel grateful. When responsibility for all activities is clearly defined and when access to company assets is carefully controlled, the honest employees can demonstrate their honesty. When all employees are considered to be honest, on the other hand, and no controls exist, all employees are unfairly tainted when one among them is dishonest.
Medaid is a medical office management franchise. There are currently twenty-five medical offices managed by a Medaid franchisee. One of the services provided to franchisees is assistance in training various staff members.

Medaid is preparing a manual for the front office staff to use as a reference guide. It will be used in training new employees as well. One of the reasons the manual is being prepared is to stress the importance of strong internal controls.

**Required:**
Prepare a short paragraph, to be included in the training materials, describing the benefits of sound internal control, from the viewpoint of the employee.

**Solution 203**
All the controls discussed in this manual may seem unnecessary to you. It may also seem that management trusts no one. However, these practices and procedures actually benefit you, the employee. First, internal control policies clearly outline who is to be responsible for various activities, such as making the daily deposit of cash in the bank. If a problem arises regarding a deposit, it is very clear to whom the company should turn to resolve the problem. If correct procedures were not followed, blame is not placed on all employees. Only those who did not follow correct procedures are held accountable for their actions. Also, strong internal controls discourage many opportunistic people, who find such opportunities to harm the company are extremely limited. Finally, all these systems, practices, and procedures result in a well-managed company that is less likely to suffer unnecessary losses, and a much better place for you to work and build a career.