

Chapter 8

CASH AND INTERNAL CONTROLS

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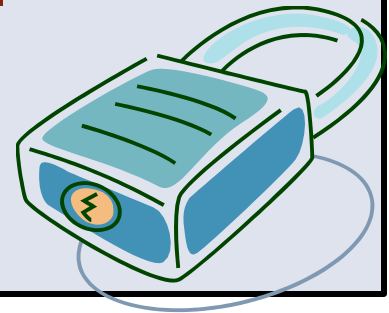
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PRINCIPLES OF INTERNAL CONTROL

Internal control principles common to all companies:

1. Establish responsibilities.
2. Maintain adequate records.
3. Insure assets and bond key employees.
4. Separate recordkeeping from custody of assets.
5. Divide responsibility for related transactions.
6. Apply technological controls.
7. Perform regular and independent reviews.



LIMITATIONS OF INTERNAL CONTROL

Human Error



Negligence
Fatigue
Misjudgment
Confusion

Human Fraud



Intent to
defeat internal
controls for
personal gain

Human fraud triple-threat:
Opportunity, Pressure, and Rationalization.

CONTROL OF CASH

An effective system of internal control that protects cash and cash equivalents should meet three basic guidelines:

Handling cash is separated from recordkeeping for cash.

Cash receipts are promptly deposited in a bank.

Cash disbursements are made by check.



CASH, CASH EQUIVALENTS, AND LIQUIDITY

Cash and similar assets are called liquid assets because they can be readily used to settle such obligations.

Cash

Currency, coins and amounts on deposit in bank accounts, checking accounts, and some savings accounts. Also includes items such as customer checks, cashier checks, certified checks, and money orders.

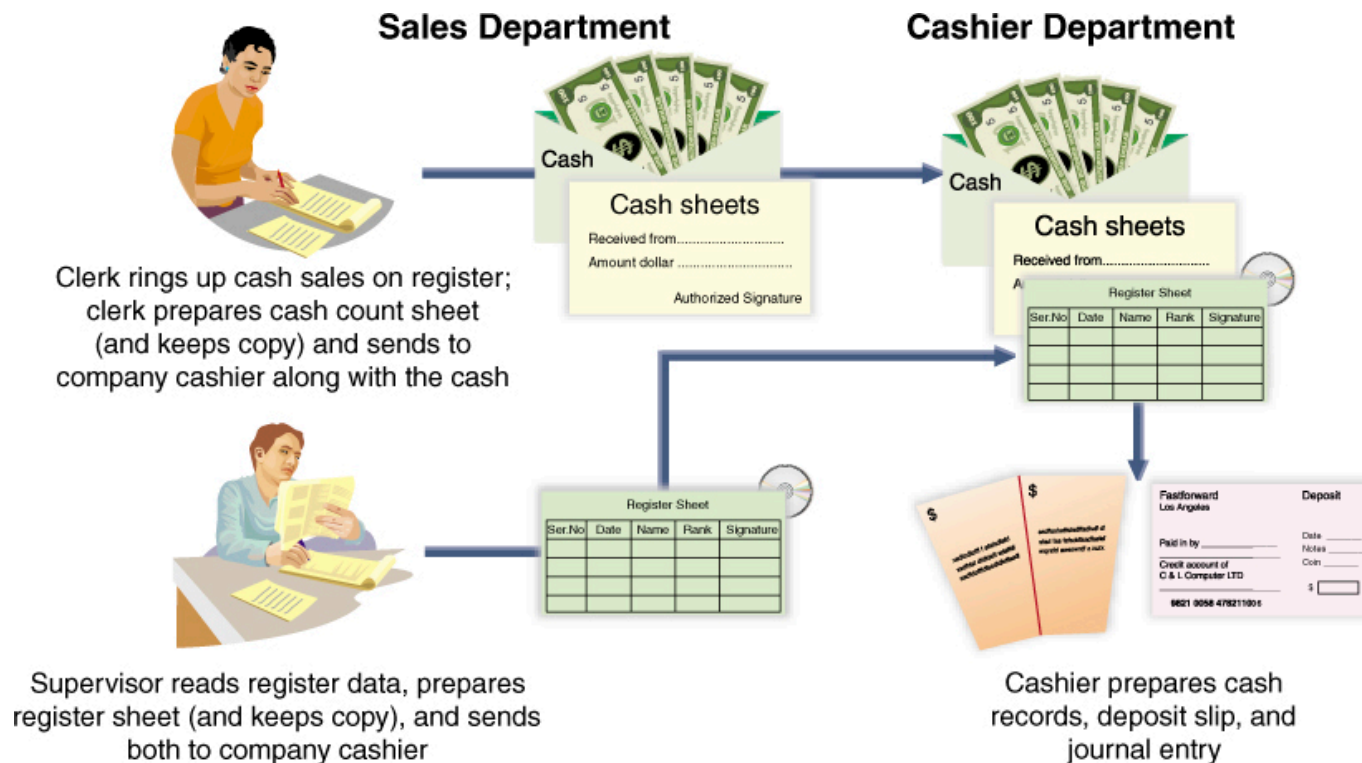
Cash Equivalents

Short-term, highly liquid investments that are:

1. Readily convertible to a known cash amount.
2. Close to maturity date and not sensitive to interest rate changes.

OVER-THE-COUNTER CASH RECEIPTS

This graphic illustrates that none of the people involved can make a mistake or divert cash without the difference being revealed.



CASH RECEIPTS BY MAIL

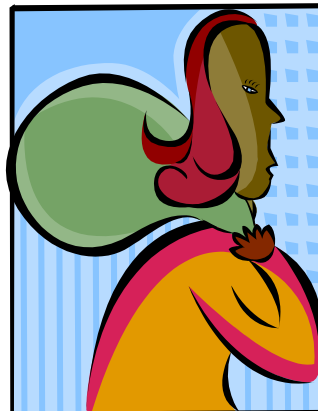
Preferably, two people are assigned the task of opening the mail.

The cashier deposits the money in a bank.

The recordkeeper records the amounts received in the accounting records.



Mailroom



Cashier



Recordkeeper

CONTROL OF CASH DISBURSEMENTS

Control of cash disbursements is especially important as most large thefts occur from payment of fictitious invoices.



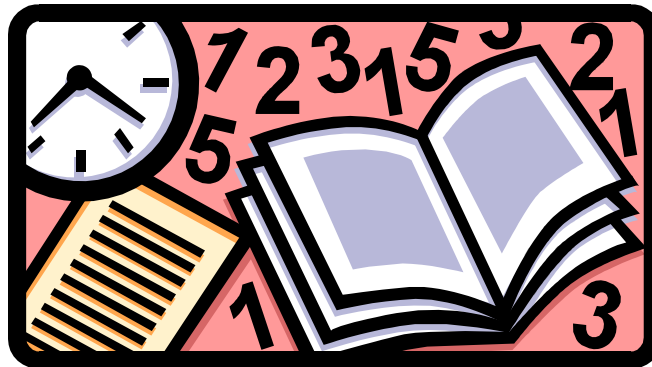
Keys to Controlling Cash Disbursements

- ❑ Require all expenditures to be made by check.
- ❑ Limit access to checks except for those who have the authority to sign checks.

VOUCHER SYSTEM OF CONTROL

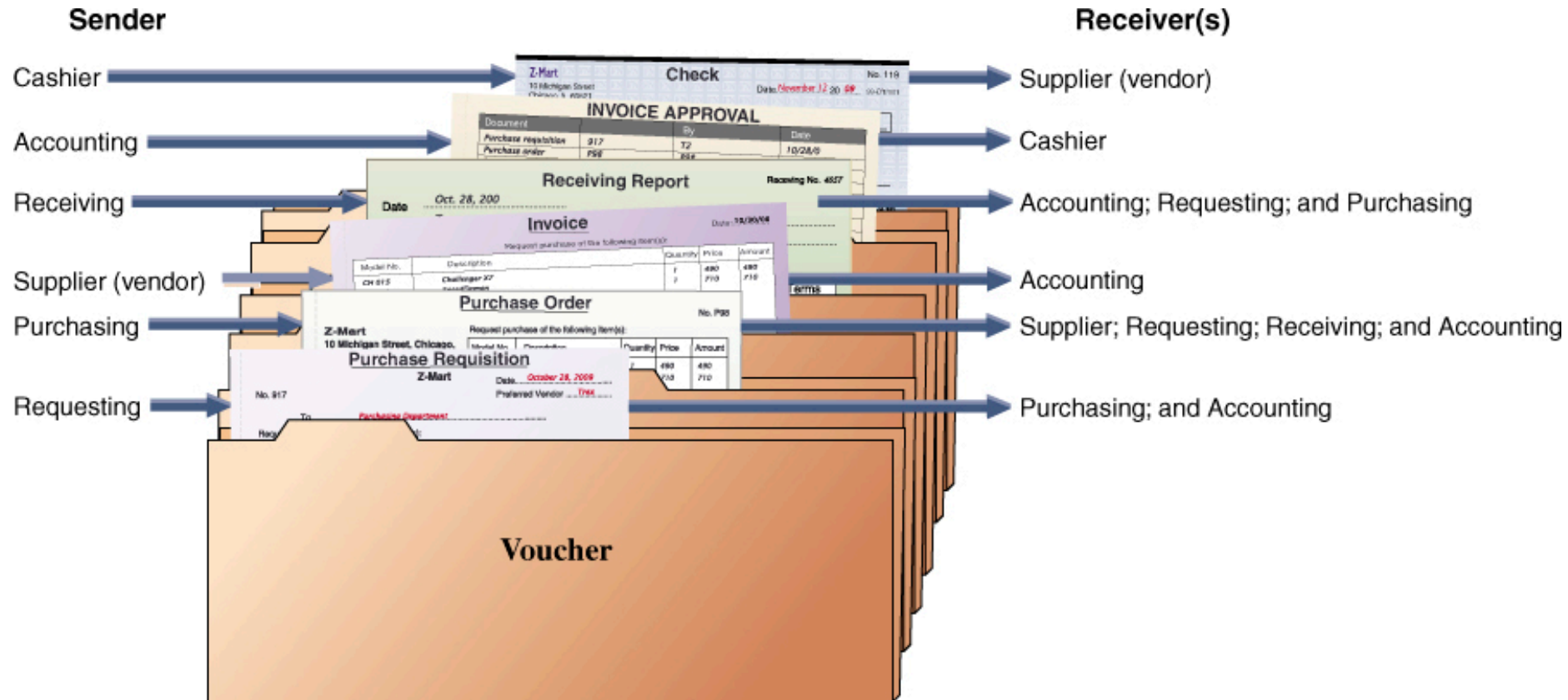
A voucher system establishes procedures for:

1. Verifying, approving, and recording obligations for eventual cash disbursements.
2. Issuing checks for payment of verified, approved, and recorded obligations.



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VOUCHER SYSTEM OF CONTROL




PETTY CASH SYSTEM OF CONTROL

Small payments required in most companies for items such as postage, courier fees, repairs, and supplies.



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BANK STATEMENT



Member FDIC

VideoBuster Company
901 Main Street
Hillcrest, NY 11749

Bank Statement

October 31, 2011
Statement Date

494 504 2
Account Number

Previous Balance	Total Checks and Debits	Total Deposits and Credits	Current Balance
1,609.58	723.00	1,163.42	2,050.00

Checks and Debits			Deposits and Credits		Daily Balance	
Date	No.	Amount	Date	Amount	Date	Amount
10/03	119	55.00	10/02	240.00	10/01	1,609.58
10/09	120	200.00	10/09	180.00	10/02	1,849.58
10/10	121	120.00	10/15	100.00	10/03	1,794.58
10/12		23.00 DM	10/16	150.00	10/09	1,774.58
10/14	122	70.00	10/23	485.00 CM	10/10	1,654.58
10/16	123	25.00	10/31	8.42 IN	10/12	1,631.58
10/23	125	15.00			10/14	1,561.58
10/25		20.00 NSF			10/15	1,661.58
		10.00 DM			10/16	1,786.58
10/26	127	50.00			10/23	2,256.58
10/29	128	135.00			10/25	2,226.58
					10/26	2,176.58
					10/29	2,041.58
					10/31	2,050.00

Symbols: **CM**—Credit Memo **EC**—Error Correction **NSF**—Non-Sufficient Funds **SC**—Service Charge
DM—Debit Memo **IN**—Interest Earned **EFT**—Electronic Funds Transfer **OD**—Overdraft

< Reconcile the account immediately. >

Usually once a month, the bank sends each depositor a bank statement showing the activity in the account.

BANK RECONCILIATION

A bank reconciliation is prepared periodically to explain the difference between cash reported on the bank statement and the cash balance on company's books.

Bank Balance			Bank Reconciliation				Book Balance		
Bank Statement			Bank balance.....	#	Book balance.....	#	Cash Account		
Checks & debits	#		Add & deduct:		Add & deduct:		Cash receipts	#	
Deposits & credits....	#		• Timing differences	#	• Timing differences	#	Cash disbursements		#
Balance.....	#		• Any errors	#	• Any errors	#	Balance	#	
			Adjusted bank bal.....	#	Adjusted book bal.....	#			



BANK RECONCILIATION

The balance of a checking account reported on the bank statement rarely equals the balance in the depositor's accounting records.

Cash Balance per Bank

+ Deposits in Transit

- Outstanding Checks

+/- Errors

Adjusted Cash Balance

=

Cash Balance per Book

+ Collections & Interest

- Uncollectible items

+/- Errors

Adjusted Cash Balance

Adjusting entries are recorded for the reconciling items on the **book** side of the reconciliation.



GLOBAL VIEW

Internal Control Purposes, Principles and Procedures

The purposes and principles of internal control systems are fundamentally the same across the globe.

Control of Cash

Accounting definitions for cash are similar for U.S. GAAP and IFRS.

Banking Activities as Controls

There is a global demand for banking services, bank statements, and bank reconciliations. To the extent feasible, companies utilize banking services as part of their effective control procedures.

APPENDIX 8A: DOCUMENTATION AND VERIFICATION

Purchase Requisition

Purchase Order

Invoice

Receiving Report



END OF CHAPTER 8

