

- h. You reviewed the company's policy and procedures manual, which listed policies for dealing with customers, vendors, and employees.
- i. Your preliminary assessment is that the accounting systems are well designed and employ effective internal control procedures.
- j. Some employees complained that some managers would, on occasion, contradict the instructions of other managers regarding proper data security procedures.
- k. After a careful review of the budget for data security enhancement projects, you feel it appears to be adequate.
- l. The new information systems project for an enhanced network firewall appeared to be on a very aggressive implementation schedule. The manager for IT mentioned that even if he put all of his personnel on this project for the next five weeks, he still would not be able to complete the project in time. The manager has mentioned this to company management, which seems unwilling to modify the schedule.
- m. Several new employees have had trouble completing some of their duties, and they do not appear to know who to ask for help.
- n. Go-Go's strategy is to achieve consistent growth for its shareholders. However, its policy is to not invest in any project unless its payback period is no more than 48 months and yields an internal rate of return that exceeds its cost of capital by 3%.
- o. You observe that company purchasing agents wear clothing and exhibit other paraphernalia from major vendors. Also, while interviewing the purchasing department manager, you notice a picture on his desk of him holding a big fish on the deck of a very nice fishing boat that has the logo of a major Go-Go vendor painted on its wheelhouse.

### Required

The information you have obtained suggests potential problems relating to one or more elements of Go-Go's internal environment. Identify the problems and explain them in relation to the internal environment concepts discussed in this chapter.

**6.2** Explain how the principle of separation of duties is violated in each of the following situations. Also suggest one or more procedures to reduce the risk and exposure highlighted in each example.

- a. A payroll clerk recorded a 40-hour work week for an employee who had quit the previous week. He then prepared a paycheck for this employee, forged her signature, and cashed the check.
- b. While opening the mail, a cashier set aside, and subsequently cashed, two checks payable to the company on account.
- c. A cashier prepared a fictitious invoice from a company using his brother-in-law's name. He wrote a check in payment of the invoice, which the brother-in-law later cashed.
- d. An employee of the finishing department walked off with several parts from the storeroom and recorded the items in the inventory ledger as having been issued to the assembly department.
- e. A cashier cashed a check from a customer in payment of an account receivable, pocketed the cash, and concealed the theft by properly posting the receipt to the customer's account in the accounts receivable ledger.
- f. Several customers returned clothing purchases over a week's time. Instead of putting the returned clothing into a return bin to be put back on the rack, a clerk put the clothing in a separate bin under some cleaning rags. After her shift, she transferred the clothes to a gym bag and took them home.
- g. A receiving clerk noticed that four cases of MP3 players were included in a shipment when only three were ordered. The clerk put the extra case aside and took it home after his shift ended.
- h. An insurance claims adjuster had check signing authority of \$6,000. The agent created three businesses that subsequently billed the insurance company for

work not performed on legitimate insurance claims. The agent signed the checks for the invoices. The invoices never exceeded \$6,000.

- i. An accounts receivable clerk recorded invoices received from a company that he and his wife own and authorized their payment.
- j. A cashier created false purchase return vouchers to hide his theft of several thousand dollars from his cash register.
- k. A purchasing agent received a 10% kickback of the invoice amount for all purchases made from a specific vendor.

**6.3** The following description represents the policies and procedures for agent expense reimbursements at Excel Insurance Company.

Agents submit a completed expense reimbursement form to their branch manager at the end of each week. The branch manager reviews the expense report to determine if the claimed expenses are reimbursable based on the company's expense reimbursement policy statements and reasonableness of amount. Company policy states that agents are to document any questionable expense item and the branch manager must approve in advance expenditures exceeding \$500.

After the expenses are approved, the branch manager sends the expense report to the home office, where accounting records the transaction and cash disbursements prepares the expense reimbursement check. Cash disbursements sends the expense reimbursement checks to the branch manager, who distributes them to the agents.

To receive cash advances for anticipated expenses, agents must complete a Cash Advance Approval form. The branch manager reviews and approves the Cash Advance Approval form and sends a copy to accounting and another to the agent. The agent submits the copy of the Cash Advance Approval form to the branch office cashier to obtain the cash advance.

At the end of each month, internal audit at the home office reconciles the expense reimbursements. It adds the total dollar amounts on the expense reports from each branch, subtracts the sum of the dollar totals on each branch's Cash Advance Approval form, and compares the net amount to the sum of the expense reimbursement checks issued to agents. Internal audit investigates any differences.

- Identify the internal control strengths and weaknesses in Excel's expense reimbursement process.

*(CMA Examination, adapted)*

**6.4** The Gardner Company, a client of your firm, has come to you with the following problem: It has three clerical employees who must perform the following functions:

- a. Maintain the general ledger
- b. Maintain the accounts payable ledger
- c. Maintain the accounts receivable ledger
- d. Prepare checks for signature
- e. Maintain the cash disbursements journal
- f. Issue credits on returns and allowances
- g. Reconcile the bank account
- h. Handle and deposit cash receipts

Assuming equal abilities among the three employees, the company asks you to assign the eight functions to them to maximize internal control. Assume that these employees will perform no accounting functions other than the ones listed.

#### Required

- a. List four possible unsatisfactory pairings of the functions.
- b. State how you would distribute the functions among the three employees. Assume that with the exception of the nominal jobs of the bank reconciliation and the issuance of credits on returns and allowances, all functions require an equal amount of time.

*(CPA Examination, adapted)*