

ACC101 – CHAPTER 6

Accounting Cash and Internal Controls



The Bank Reconciliation

The balance according to the bank statement and the balance according to the depositor's records must be adjusted in order to accurately compute the cash balance. Each balance is adjusted for items not previously recorded as follows:

<u>Bank's Balance</u>		<u>Depositor's Balance</u>	
Add:	Deposits in Transit	Add:	Notes collected by the bank
	Errors		Errors
Deduct:	Outstanding Checks	Deduct:	Service Charges
	Errors		NSF checks
			Errors

** All adjustments to the depositor's balance MUST be journalized in order for the cash account in the ledger to agree with the adjusted cash balance. **

Example #1

The cash account for Ace Co. on August 31, 2004, indicated a balance of \$9,420. The bank statement indicated a balance of \$12,785 on August 31, 2004. The following reconciling items were discovered.

- Checks outstanding totaled \$6,240.
- A deposit of \$5,375, representing cash receipts of August 31, had been made too late to appear on the bank statement.
- A check for \$240 had been incorrectly charged by the bank as \$420.
- A check for \$658 returned with the statement had been recorded by Ace as \$568. The check was for the payment of an obligation to Cahill Co. on account.
- The bank had collected for Ace \$2,800 on a note left for collection. The face of the note was \$2,000.
- Bank service charges for August amounted to \$30.

Prepare the bank reconciliation in good form and journalize the necessary entries.

Solution #1

Ace Company
Bank Reconciliation
August 31, 2004

Cash balance according to bank statement		\$12,785
Add: Deposit of August 30 not recorded by bank	\$5,375	
Bank error	<u>180</u>	<u>5,555</u>
		\$18,340
Deduct: Outstanding checks		<u>6,240</u>
Adjusted balance		<u>\$12,100</u>
Cash balance according to depositor's records		\$9,420
Add: Proceeds of note and interest collected by bank		<u>2,800</u>
		12,220
Deduct: Error in recording check	90	
Bank service charges	<u>30</u>	<u>120</u>
Adjusted balance		<u>\$12,100</u>

Journal entries

Cash	2,800	
Notes Receivable		2,000
Interest Revenue		800
A/P-Cahill Co.	90	
Misc. Adm. Expense	30	
Cash		120

Practice Problem #1

The cash account for Kahn Inc. on November 30, 2003, indicated a balance of \$5,699. The bank statement indicated a balance of \$13,167 on November 30, 2003. The following reconciling items were discovered.

- a. Checks outstanding totaled \$5,175.
- b. A deposit of \$3,842, representing cash receipts of November 30, had been made too late to appear on the bank statement.
- c. The bank had collected for Kahn \$4,800 on a note left for collection. The face of the note was \$4,200.
- d. Kahn had recorded a check for \$2,040 returned with the statement as \$2,400. The check was for the payment of a 3-year insurance policy.
- e. A check for \$1,176 had been incorrectly charged by the bank as \$176.
- f. Bank service charges for November amounted to \$25.

Prepare the bank reconciliation and journalize the necessary entries.

Petty Cash

A Petty Cash fund is used to provide small amounts of cash for common expenditures for which the company does not write a check or purchase on account. Examples include employee birthday cakes, office supplies or postage due on mail.

Petty cash funds are typically operated on an *imprest* basis, meaning that when cash is expended from the fund, it is replaced by a receipt in the same amount. The balance of an imprest fund should always equal the balance established for the fund.

The petty cash account always has an entry to establish the fund and perhaps a subsequent entry to increase or decrease the fund's balance. Replenishment entries are not recorded using the petty cash account. Any differences between the total of the receipts for funds expended and the amount necessary to replenish the fund balance are debited or credited to the Cash Short and Over account.

Petty Cash	200	<i>To establish the fund</i>
Cash	200	
Store Supplies	95	<i>To replenish the fund and</i>
Delivery Expense	42	<i>record all the</i>
Misc. Adm. Expense	38	<i>expenses paid for in cash.</i>
Cash	175	

Practice Problem #2

Journalize the following transactions. (Use Cash Short and Over if you are short or over in the petty cash fund.)

- June 1: Established a petty cash fund of \$500
- 22: Petty cash on hand was \$54. Replenish the petty cash fund for the following disbursements, each evidenced by a petty cash receipt:
- July 3: Store supplies \$120.75
- 5: Express charges on merchandise purchased F.O.B. shipping point, \$150.25
- 6: Postage stamps, \$44 (Office Supplies)
- 7: Office supplies, \$37.50.
- 8: Repair to computer, \$82
- 25: Increased the petty cash fund to \$600.

The Cash Short and Over Account

This account is used to record shortages or overages in the cash register. The cash in the drawer represents a debit to cash. The cash register tape represents your credit to sales. If there is a shortage, you must debit Cash Short and Over. If there is an overage, you must credit Cash Short and Over.

Cash	3,540	<i>(Cash in the drawer)</i>	Cash	5,420
Cash Short & Over	15	<i>(Shortage)</i>	Cash Short & Over	20
Sales	3,555	<i>(Cash register tape)</i>	Sales	5,400

Practice Problem #3

Journalize the following transactions.

- a. The actual cash received from cash sales was \$15,362 and the amount indicated by the cash register tape was \$15,379.
- b. The cash sales for the day, according to the cash register tapes, totaled \$8,792. The actual cash received from cash sales was \$8,801.

SAMPLE MULTIPLE CHOICE QUESTIONS

1. Procedures designed to detect theft or misuse of cash are called:
 - a. Detective controls
 - b. Cash controls
 - c. Protective controls
 - d. Accounting controls
2. A debit or credit memorandum describing entries in the depositor's bank account may be enclosed with the bank statement. Which of the following items would be reported to the depositor on a credit memorandum?
 - a. Deposited checks returned for insufficient funds
 - b. A service charge
 - c. A promissory note collected by the bank
 - d. Notification that a customer's check for \$375 was recorded by the depositor as \$735 on the deposit ticket.
3. The bank reconciliation:
 - a. Should be prepared by an employee who records cash transactions
 - b. Is for information purposes only
 - c. Is part of the internal control system
 - d. Is sent to the bank for verification

4. Receipts from cash sales of \$7,500 were recorded incorrectly in the cash receipts journal as \$5,700. This item would be included on the bank reconciliation as:
 - a. An addition to the balancer per depositor's records
 - b. An addition to the balance per bank statement
 - c. A deduction from the balance per bank statement
 - d. A deduction from the balance per depositor's records
5. Accompanying the bank statement was a debit memorandum for an NSF check received from a customer. What entry is required in the depositor's accounts?
 - a. Debit Other Income, credit Cash
 - b. Debit Cash, credit Other Income
 - c. Debit Accounts Receivable, credit Cash
 - d. Debit Cash, credit Accounts Receivable
6. A voucher
 - a. Is normally prepared in the Accounting Department
 - b. System is used to control cash receipts
 - c. Is received from customers to explain the purpose of a payment
 - d. System is an internal control procedure to verify the assets in the ledger are the ones the company owns
7. A person authorized to write checks drawn on a checking account at a bank must sign and have on file with the bank a:
 - a. Bank card
 - b. Deposit ticket
 - c. Checkbook
 - d. Signature card
8. The credit recorded in the journal to reimburse the petty cash fund is to:
 - a. Petty Cash
 - b. Accounts Receivable
 - c. Cash
 - d. Various accounts for which the petty cash was disbursed
9. Cash equivalents:
 - a. Are illegal in some states
 - b. Are highly liquid investments
 - c. Will be converted to cash within one year
 - d. Are only available to large companies

10. A minimum cash balance required by a bank is called:
 - a. Cash in the bank
 - b. Cash equivalent
 - c. EFT
 - d. Compensating balance
11. A doomsday ratio of 1.05
 - a. Means the company should immediately invest the excess cash.
 - b. Means a company has one dollar in cash and cash equivalents for every one dollar and five cents in liabilities
 - c. Means a company has one dollar and five cents in cash and cash equivalents to pay every dollar in current liabilities.
 - d. Means that current liabilities are one hundred five percent of current assts.
12. The credit balance in Cash Short and Over at the end of an accounting period is reported as
 - a. Income on the income statement
 - b. An expense on the income statement
 - c. An asset on the balance sheet
 - d. A liability on the balance sheet
13. A check drawn by a depositor for \$195 in payment of a voucher was recorded in the journal as \$915. This item would be included on the bank reconciliation as a(n):
 - a. Addition to the balance per the bank statement
 - b. Addition to the balance per the depositor's records
 - c. Deduction from the balance per the bank statement
 - d. Deduction from the balance per the depositor's records
14. Segregation of duties reduces the risk of errors and irregularities.
 - a. True
 - b. False
15. All disbursements, even for incidental amounts, must be paid by check.
 - a. True
 - b. False
16. Deposits in transit are added to the cash balance per books on a bank reconciliation.
 - a. True
 - b. False

17. Which of the following is not a principle of internal control?
- Segregation of duties
 - Documentation procedures
 - Collusion between employees
 - Bonding of employees
18. When the cashier also keeps the books for a company, which internal control principle is violated?
- Rotating employee duties
 - Establishment of responsibility
 - Segregation of duties
 - Documentation procedures
19. Springer Company had outstanding checks totaling \$4,500 on its September bank reconciliation. In October, the company issued checks totaling \$45,700. The October bank statement shows that checks totaling \$39,800 cleared the bank. In addition, a check from one of Springer's customers in the amount of \$500 was returned as NSF. The outstanding checks on the October bank reconciliation should total
- \$5,900
 - \$9,900
 - \$10,400
 - \$1,400
20. Jones Company collected the following information to prepare its May bank reconciliation:
- | | |
|--|---------|
| Cash balance per books, May 31 | \$5,300 |
| Deposits in transit | 510 |
| Notes Receivable with interest collected by bank | 580 |
| Bank Service Charges | 30 |
| Outstanding Checks | 1,800 |
| NSF check | 150 |
- The adjusted cash balance per books on May 31 is
- \$5,700
 - \$5,810
 - \$6,210
 - \$5,660

21. Barker Company collected the following information to prepare its November bank reconciliation:

Cash balance per bank, November 30 ..		\$21,000
Note Receivable plus interest collected by bank		9,000
Outstanding checks	.....	6,000
Deposit in Transit	.....	5,400
Bank Service charges	.....	85
NSF check	.....	2,100

The cash balance per books, before adjustments to the book balance is

- a. \$20,400
 - b. \$13,585
 - c. \$6,815
 - d. \$27,815
22. An adjusting entry is required for
- a. Outstanding checks
 - b. Deposits in transit
 - c. Bank errors
 - d. NSF checks
23. The following information was taken from the Carson Company cash budget for the month of April:
- | | | |
|------------------------|-------|----------|
| Beginning cash balance | ..... | \$45,000 |
| Cash Receipts | ..... | 27,000 |
| Cash Disbursements | ..... | 51,000 |

If the company has a policy of maintaining a minimum cash balance of \$37,000, the amount the company would have to borrow is

- a. \$24,000
- b. \$8,000
- c. \$16,000
- d. \$14,000

SOLUTIONS TO PRACTICE PROBLEMS

Practice Problem #1

July 1	Petty Cash	500.00	
	Cash		500.00
22	Store Supplies	120.75	
	Mdse Inventory	150.25	
	Office Supplies	81.50	
	Repair Expense	82.00	
	Cash Short & Over	11.50	
	Cash		446.00
25	Petty Cash	100.00	
	Cash		100.00

Practice Problem #2

a.	Cash	15,362	
	Cash Short & Over	17	
	Sales		15,379
b.	Cash	8,801	
	Cash Short & Over		9
	Sales		8,792

Practice Problem #3

Kahn Inc. Bank Reconciliation November 30, 2003

Cash balance according to bank statement		\$13,167
Add: Deposit of November 30 not recorded by bank		<u>3,842</u>
		\$17,009
Deduct: Outstanding checks	5,175	
Bank error	<u>1,000</u>	<u>6,175</u>
Adjusted Balance		<u>\$10,834</u>
Cash balance according to depositor's records		\$5,699
Add: Note collected by bank, including interest	4,800	
Error recording check for insurance policy	<u>360</u>	<u>5,160</u>
		\$10,859
Deduct: Bank service charges		<u>25</u>
Adjusted Balance		<u>\$10,834</u>

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Journal entries

Cash	5,160	
Notes Receivable		4,200
Interest Income		600
Prepaid Insurance		360
Misc. Adm. Expense	25	
Cash		25

SOLUTIONS TO MULTIPLE CHOICE QUESTIONS

1. A
2. C
3. C
4. A
5. C
6. A
7. D
8. C
9. B
10. D
11. C
12. A
13. B
14. A
15. B: Petty Cash is used for incidental amounts
16. B: Added to the balance per bank
17. C
18. C

19. C:	Outstanding checks for September	\$ 4,500	
	+ Checks issued in October	<u>45,700</u>	
	Total checks outstanding		50,200
	- Checks cleared on October statement		<u>39,800</u>
	Outstanding checks for October		\$10,400
20. A:	Balance per books		\$5,300
	Add: Note collected by bank		580
	Deduct: NSF check	(150)	
	Bank Service Charge	<u>(30)</u>	<u>(180)</u>
	Adjusted Balance		\$5,700

21. B:	Balance per bank	\$21,000
	Add: Deposits in Transit	5,400
	Deduct: Outstanding checks	<u>(6,000)</u>
	Adjusted Balance	\$20,400

	Balance per books	X
	Add: Note collected by bank	9,000
	$x + 9000 - 85 - 2100 = 20400$	
	Deduct: Bank Service Charge	(85)
	NSF Check	<u>(2,100)</u>
	Adjusted Balance	\$20,400
	$X + 6815 = 20,400$	
	$X = 13,585$	

22. D

23. C:	Beginning Cash Balance	\$45,000
	Plus: anticipated receipts	27,000
	Less: anticipated disbursements	<u>(51,000)</u>
	Projected ending cash balance	\$21,000

	Minimum Cash Balance	\$37,000
	Less: Projected ending cash balance	<u>21,000</u>
	Borrowing required	\$16,000