

Chapter 12—Solutions to Problems

Problem 1: Solution

1. Safeguard assets.
2. Check accuracy and reliability of accounting data.
3. Promote operational efficiency.
4. Safeguard assets.
5. Promote operational efficiency.
6. Check accuracy and reliability of accounting data.

Problem 2: Solution

1. Preventive
2. Preventive
3. Detective
4. Preventive
5. Detective

Problem 3: Solution

Critique

1. Potential lost sales because patrons may not wait; The flow of work may not be spread evenly throughout the facility; Lack of a greeting from a host/hostess may be interpreted as "not caring."
2. It appears that too many tables may be assigned to each waitperson.
3. Lack of separation of duties; Waitstaff may be ringing up sales they have recorded; Since the responsibility for the cash is spread across all who ring up sales, it is difficult to hold a single person responsible.
4. Tips belong strictly to tipped employees; By law, no portion may be retained by the employer (at least in most states).

Recommendations

1. Employ a host/hostess to greet patrons and assist in the café's operations.
2. Consider hiring more waitpersons so that better service can be provided.
3. A back-up cashier should be hired or at least one waitperson should be assigned back-up cashier responsibilities when the cashier must be away from his or her station. Or, a member of the management team could fill in for the cashier.
4. The employer is in violation of law by taking some tips. If gratuities are charged rather than tips, then the employer may retain part or even all of the gratuities charged. Switching to a gratuity approach will require some revisions in the café's compensation system.

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Problem 4: Solution

- | | <u>Preventive/Detective</u> | <u>Accounting/Administrative</u> |
|----|-----------------------------|----------------------------------|
| 1. | | |
| 1 | Preventive | Accounting |
| 2 | Preventive | Accounting |
| 3 | Detective | Accounting |
| 4 | Preventive | Accounting |
| 5 | Detective | Administrative |
| 6 | Preventive | Accounting |
| 7 | Detective | Accounting |
| 8 | Preventive | Administrative |
| 9 | Detective | Accounting |
| 10 | Preventive | Accounting |
2. All detective controls have a preventive aspect if the employees realize the detective control is in place. For example, if employees *know* the external auditor will conduct a surprise cash audit (#3), they may be more careful in handling cash.

Problem 5: Solution

| | <u>Preventive/Detective</u> | <u>Accounting/Administrative</u> |
|---|-----------------------------|----------------------------------|
| 1 | Preventive | Accounting |
| 2 | Detective | Accounting |
| 3 | Preventive | Administrative |
| 4 | Detective | Accounting |
| 5 | Preventive | Accounting |
| 6 | Preventive | Accounting |
| 7 | Preventive | Administrative |
| 8 | Preventive | Accounting |

Problem 6: Solution

1. Sunrise Corporation (Internal)
2. Green and White (External)
3. Sunrise Corporation (internal)
4. Green and White (External)
5. Sunrise Corporation (Internal)
6. Green and White (External)
7. Sunrise Corporation (Internal)

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Problem 7: Solution

1. Several deficiencies include the following:
 - Lack of segregation of duties: Bookkeeper is handling cash as well as accounts receivable. The bookkeeper who is responsible for the receipts is preparing the bank reconciliation.
 - Auditor lacks persistence required of individuals performing independent checks.
 - There is apparently no fidelity bond coverage.

2. Suggestions to improve the system include the following:
 - The tasks of accounting for receivables and handling cash receipts should be segregated.
 - The person responsible for cash receipts should not be preparing the bank reconciliation.
 - Auditors should be better trained and instructed as to their responsibility to detect fraud.
 - At a minimum, fidelity bond coverage should be obtained on all personnel in positions of trust.

Problem 8: Solution

1. Petty Cash Reconciliation

| | | |
|-----------------------------------|-------------|----------------|
| Cash Balance @ 8/15 | | \$ 25.00 |
| Less: | | |
| Postage | \$15.00 | |
| Fuel for Lawn Mower | 10.50 | |
| Contribution to Boy Scouts | 25.00 | |
| Postage due for Supplies Delivery | 8.20 | |
| Taxi | 12.50 | |
| Ink Pens | 8.60 | |
| Freight on Equipment Delivery | 32.80 | |
| Donuts for Office Staff | <u>9.50</u> | <u>122.10</u> |
| Total | | 147.10 |
| Book Balance @ 8/15 | | <u>150.00</u> |
| Cash Shortage | | <u>\$ 2.90</u> |

2. Recommendation: The disbursements from the petty cash funds should be supported by cash register tapes, invoices, or other documents. In addition, the money going into or out of the petty cash fund should be counted more carefully and regular monitoring should occur on more frequent intervals, such as weekly or daily.

3. Journal Entry

| | | |
|--------------------------|----------|----------|
| Various Expense Accounts | \$125.00 | |
| Cash | | \$125.00 |

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Problem 9: Solution

| | | | |
|---------------------------|--------------|-----------------------|--------------------|
| Bank balance 1/31/X2 | | | \$13,424.15 |
| Less: Outstanding checks: | | | |
| | <u>Chk.#</u> | <u>Amount</u> | |
| | 1059 | \$ 246.81 | |
| | 1072 | 2,621.00 | |
| | 1073 | 349.06 | |
| | 1074 | 15.92 | |
| | 1075 | 1,123.46 | |
| | 1076 | <u>998.43</u> | (5,354.68) |
| Add: Service charge | | \$ 32.46 ¹ | |
| Insufficient funds check | | 168.24 | |
| Deposit in transit | | 2,149.83 | <u>2,350.53</u> |
| Book balance 1/31/X2 | | | <u>\$10,420.00</u> |

¹This amount will be recorded as expense in February 20X2.

Problem 10: Solution

1. 28.71%*
2. 27.49%**
3. 30.41%***

| | | |
|--------------------------------|--|-------------------------------|
| Sales: | | Cost of Sales: |
| \$4.95 × 50 = \$ 247.50 | | \$1.60 × 50 = \$ 80.00 |
| \$4.45 × 100 = \$ 445.00 | | \$1.40 × 100 = \$140.00 |
| \$3.95 × 150 = \$ 592.50 | | \$0.95 × 150 = \$142.50 |
| \$4.95 × 80 = \$ 396.00 | | \$1.70 × 80 = \$136.00 |
| \$2.95 × 40 = \$ <u>118.00</u> | | \$0.45 × 40 = \$ <u>18.00</u> |
| \$1,799.00 | | \$516.50 |

* $[(1.6 + 1.4 + 0.95 + 1.7 + 0.45)/5] \div [(4.95 + 4.45 + 3.95 + 4.95 + 2.95)/5] = \underline{28.71\%}$

** $[(1.6/4.95) \times 0.2] + [(1.4/4.45) \times 0.2] + [(0.95/3.95) \times 0.2] + [(1.7/4.95) \times 0.2] + [(0.45/2.95) \times 0.2] = \underline{27.49\%}$

*** $547/1,799 = \underline{30.41\%}$

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Problem 11: Solution

| | | | |
|--|-------------|---------------|--------------------|
| Bank balance—December 31, 20X1 | | | \$ 7,432.00 |
| Less: Outstanding checks: | <u>Ck.#</u> | <u>Amount</u> | |
| | 8923 | \$100.10 | |
| | 8936 | 248.15 | |
| | 9164 | 384.21 | |
| | 9173 | 439.42 | |
| | 9190 | 526.14 | |
| | 9191 | 422.15 | |
| | 9192 | <u>67.42</u> | \$(2,187.59) |
| Add: Deposit in transit | | | 1,221.75 |
| Add: Insufficient funds check redeposited | | | <u>57.18</u> |
| General checking account balance--12/31/X1 | | | <u>\$ 6,523.34</u> |

Problem 12: Solution

1. How to split Harris's duties between two people:

| <u>Employee A</u> | <u>Employee B</u> |
|--------------------------|---|
| (a) handle cash receipts | --- |
| (b) prepare all checks | distribute all checks |
| (c) --- | sign checks in owner's/manager's absence |
| (d) --- | prepare bank reconciliation |
| (e) --- | handle accounts receivable |

2. The owner/manager should:
- 1) Distribute all payroll checks.
 - 2) Prepare the bank reconciliation.
 - 3) Sign all checks. (Do not have checks signed during absences except in extremely rare circumstances.)

Problem 13: Solution

Internal control can be strengthened as follows:

- Use individual registration cards, and check identification as necessary.
- Provide receipts to all departing guests.
- Determine the planned departure date when a guest checks in, and note this on the registration card.
- Ask how guests plan to pay the hotel bill, and note this on the registration card. If cash is to be used, offer to take cash at registration.
- Have standard follow-up procedures for "skippers."

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Problem 14: Solution

The action and proposal by Gerald Reeves may have serious ethical implications. It is clear Reeves has selected his best maintenance worker for his high quality of work. However, labeling this maintenance worker as the best can result in tension at the workplace amongst other maintenance employees if they know about the situation. In addition, if the best maintenance employee does not perform to standards on Reeves's house, the general manager may show negative emotions towards the maintenance worker he once perceived as the best. The final ethical implication is the issue of money. Reeves has offered to pay the employee equal to his wages at the hotel. Is this fair compensation for work performed on a personal home, or is this a far cheaper deal for Reeves?

Due to the above, Reeves should avoid employing the hotel's personnel for personal services.

Problem 15: Solution

1. Weaknesses in internal control include the following:
 - Lack of segregation of duties: The payroll supervisor should not be reconciling the payroll account if he is signing payroll checks. People with accounting responsibilities ideally should not be handling cash or signing checks.
 - Blank checks should not be signed in advance.
2. The theft could have been prevented as follows:
 - Not providing the payroll supervisor with signed checks.
 - Having someone other than the payroll supervisor reconcile the payroll account. This would not allow the cover-up.

Problem 16: Solution

The suggestion by Ryan Quick for Carrie to perform numerous payroll functions does not take into consideration the need for internal controls to maintain accuracy. Carrie may continue to recheck the hours worked by employees as a form of confirming the precision of reported hours worked by other associates. Carrie may also continue to prepare the payroll accounts. If she maintains this task, Carrie should no longer sign the checks. This task could be transferred to the hotel's controller or even the general manager. Carrie should also not prepare the bank reconciliation for the payroll bank account, although she could review the prepared report. One of the associates in the accounting department could easily prepare the statement. The purpose behind segregating the tasks allows for more individuals to oversee the payroll process and monitor for errors, fraud, or embezzlement.

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Problem 17: Solution

1.
 - a. Failure to record extra charges prior to the guest check
 - b. Lack of separation of duties--the same person records the room charges and receives the cash
 - c. No set procedure to strongly encourage the guest to take the receipted statement
 - d. No procedure for supervisory approval to drop extra charge
2.
 - a. Charges should be recorded by billing clerk.
 - b. The cashier should only record cash received.
 - c. All extra charges waived should be approved by supervisory personnel.
 - d. There should be a procedure to strongly encourage guests to take their statements.

Problem 18: Solution

1. Bank reconciliation:

| | |
|----------------------------------|-------------------|
| Bank balance at December 31 | \$2,134.98 |
| Cash in transit | 2,400.28 |
| Outstanding checks: | |
| ck. 2186 | \$349.00 |
| ck. 2212 | 94.51 |
| ck. 2376 | 153.40 |
| ck. 2377 | 146.18 |
| ck. 2378 | 349.00 |
| | (1,092.09) |
| Bank service charges | 22.47 |
| Checks returned by the bank: | |
| James Jones | 68.21 |
| Wilma Hill | 157.83 |
| Balance per books at December 31 | <u>\$3,691.68</u> |

2. Adjusting entries:

| | | |
|---------------------|----------|--------|
| Banking charges | \$ 22.47 | |
| Accounts receivable | 226.04 | |
| Cash | | 248.51 |

To record bank charges for December and to record checks returned by the bank.

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Problem 19: Solution

Bank Reconciliation
Sundowner Café
September 30, 20X2

| | | |
|----------------------------------|---------------|------------------------|
| Bank Balance @ 9/30/X2 | | \$2,100.50 |
| Add: Deposit in Transit | | 855.00 |
| Less: Outstanding Checks | | |
| Ck. 1152 | \$ 150.00 | |
| Ck. 1188 | 1,258.54 | |
| Ck. 1195 | <u>321.80</u> | (1,730.34) |
| Other: | | |
| Insufficient Funds Check | | 135.15 |
| Service Charges | | 8.00 |
| New General Account Checks | | <u>125.50</u> |
| Cash Balance Per Books @ 9/30/X2 | | <u><u>1,493.81</u></u> |

2. Adjusting Entry

| | | |
|----------------------------------|----------|----------|
| Accounts Receivable-(M.J. Smith) | \$135.15 | |
| Accounting Supplies | 125.50 | |
| Service Charges | 8.00 | |
| Accounts Payable | | \$268.65 |

Problem 20: Solution

1. Weaknesses:

- Lack of separation of duties, including bookkeeping and cash responsibilities and mail-opening responsibilities related to collections. Remittances are handled by the chief accountant. Also, protests from former guests were handled by personnel responsible for preparation of offending documents.
- Failure to have an external audit of the hotel.
- Key employees with cash responsibilities are not required to take vacations.

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Problem 20: Solution (continued)

2. Recommendations:

Separation of duties:

- Accounting and cash responsibilities should be separated.
- The mail should be opened by someone in the manager's office, and a record of the mail should be made in triplicate (as suggested in the case).
- Guest protests regarding their statements should be reviewed by someone independent of the person preparing the statements.

External audit: An external audit should be conducted annually since procedures performed by the auditor, such as confirmation of accounts receivable, would most likely have shed light on the fraud at the time of the audit.

Required vacations: All key employees, especially those with cash responsibilities, must be required to take a vacation. During their absence, other employees should be assigned their responsibilities. If this were the rule at the hotel in the case, the fraud perpetrated by the chief accountant would have been revealed.