CA FINAL

RISK MANAGEMENT

IN-HOUSE

CASE STUDY SERIES

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Case Study 4 Questions

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Part 1: Cash

Facts: Happy Auditors LLP is preparing to conduct a walk-through of the internal controls of Big Business Inc. Based on its understanding of internal controls of prior year and initial risk assessment procedures, the company has identified the following risks related to cash:

- Kiting by the accounting department
- Inappropriate payment of personal (nonbusiness) costs
- Recording fictitious cash receipts

Big Business provides the following control narrative related to cash.

Cash Receipts:

The receptionist opens the mail and prepares a cash receipts form and a deposit slip. The receptionist provides a copy of the cash receipts form to accounting and treasury. Accounting enters the cash receipts into the general ledger from the check stubs (remittance advices). Treasury does not have access to the general ledger cash receipts program. Treasury deposits the checks at the bank daily.

Cash Disbursements:

Big Business uses the disbursement module of its ERP system to print checks. Treasury prints checks based on the due date in the system and then matches the checks to the appropriate support (invoice, receiving report, purchase order). The checks are then given to the controller and CFO for approval and signature. After the checks are signed, they are given to the receptionist for mailing, and the support is returned to AP for filing.

Overall:

Staff accountants reconcile the bank statement on a monthly basis, and the controller reviews the reconciliation.

Required:

Identify the controls that Happy Auditor should walk through to mitigate the risks identified.

1. **Kiting by the accounting department**
    a. Segregation of duties
    b. Only controller has access to inventory ledger for changes
    c. LCM analysis (independent report)
    d. Review and approval of checks and support
    e. Three-way match in AP (purchase order, receiving report, invoice)
    f. Treasury does not have access to record cash receipts in the ledger
    g. Annual inventory count (independent firm)
    h. Bank reconciliation
    i. Receiving department counts receipt of inventory purchases

2. **Inappropriate payment of personal (nonbusiness) costs**
    a. Segregation of duties
    b. Only controller has access to inventory ledger for changes
    c. LCM analysis (independent report)
    d. Review and approval of checks and support
    e. Three-way match in AP (purchase order, receiving report, invoice)
    f. Treasury does not have access to record cash receipts in the ledger
    g. Annual inventory count (independent firm)
    h. Bank reconciliation
    i. Receiving department counts receipt of inventory purchases

3. **Recording fictitious cash receipts**
    a. Segregation of duties
    b. Only controller has access to inventory ledger for changes
    c. LCM analysis (independent report)
    d. Review and approval of checks and support
    e. Three-way match in AP (purchase order, receiving report, invoice)

f. Treasury does not have access to record cash receipts in the ledger

g. Annual inventory count (independent firm)

h. Bank reconciliation

i. Receiving department counts receipt of inventory purchases

Part 2: Inventory

Facts: Based on an understanding of the internal controls of the prior year and the initial risk assessment procedures, the auditor has identified the following risks related to inventory:

- Improper valuation
- Employee theft

Big Business provides the following control narrative related to inventory.

Inventory

Inventory is ordered by the strategic planning department using a purchase order created through the system and approved by the VP Supply Chain. Upon receipt, the receiving department counts the inventory and sends a copy of the count and receiving report to accounting. AP matches the PO, invoice, and receiving report prior to payment.

Each quarter, warehouse employees perform a physical inventory count on all items. The physical inventory count is reconciled to the perpetual inventory subledger. Annually, the company hires an external inventory firm to perform the inventory count for the final fiscal period. All variances are researched while the external inventory firm is on site. Only the controller can access and make changes to the inventory ledger.

The CFO reviews product margins by product line each quarter. In addition, the VP of Supply Chain reviews and approves the final priced inventory listing. He or she is responsible for preparing the estimated excess and obsolete inventory report and presenting it to the CFO and CEO. Included in his or her report is information about excess, slow-moving, obsolete, and defective inventories. The CFO uses the report to perform a LCM analysis.

Required:

Identify the controls that Happy Auditor should walk through to mitigate the risks identified

1. **Improper valuation**
    a. Segregation of duties
    b. Only controller has access to inventory ledger for changes
    c. LCM analysis (independent report)
    d. Review and approval of checks and support
    e. Three-way match in AP (purchase order, receiving report, invoice)
    f. Treasury does not have access to record cash receipts in the ledger
    g. Annual inventory count (independent firm)
    h. Bank reconciliation
    i. Receiving department counts receipt of inventory purchases

2. **Employee theft**
    a. Segregation of duties
    b. Only controller has access to inventory ledger for changes
    c. LCM analysis (independent report)
    d. Review and approval of checks and support
    e. Three-way match in AP (purchase order, receiving report, invoice)
    f. Treasury does not have access to record cash receipts in the ledger
    g. Annual inventory count (independent firm)
    h. Bank reconciliation
    i. Receiving department counts receipt of inventory purchases