


## Chapter 08

### Special Activities

#### SA 8-1 Ethics and professional conduct in business



During the preparation of the bank reconciliation for New Concepts Co., Peter Fikes, the assistant controller, discovered that City National Bank incorrectly recorded a \$710 check written by New Concepts Co. as \$170. Peter has decided not to notify the bank but wait for the bank to detect the error. Peter plans to record the \$540 error as Other Income if the bank fails to detect the error within the next three months.

 Discuss whether Peter is behaving in a professional manner.

#### SA 8-2 Internal controls

The following is an excerpt from a conversation between two sales clerks, Ross Maas and Shu Lyons. Both Ross and Shu are employed by Hawkins Electronics, a locally owned and operated electronics retail store.

*Ross:* Did you hear the news?

*Shu:* What news?

*Ross:* Jane and Rachel were both arrested this morning.

*Shu:* What? Arrested? You're putting me on!

*Ross:* No, really! The police arrested them first thing this morning. Put them in handcuffs, read them their rights—the whole works. It was unreal!

*Shu:* What did they do?

*Ross:* Well, apparently they were filling out merchandise refund forms for fictitious customers and then taking the cash.

*Shu:* I guess I never thought of that. How did they catch them?

*Ross:* The store manager noticed that returns were twice that of last year and seemed to be increasing. When he confronted Jane, she became flustered and admitted to taking the cash, apparently over \$7,000 in just three months. They're going over the last six months' transactions to try to determine how much Rachel stole. She apparently started stealing first.

 Suggest appropriate control procedures that would have prevented or detected the theft of cash.

**SA 8-3**  
Internal controls

The following is an excerpt from a conversation between the store manager of Yoder Brothers Grocery Stores, Lori Colburn, and Terry Whipple, president of Yoder Brothers Grocery Stores.

*Terry:* Lori, I'm concerned about this new scanning system.

*Lori:* What's the problem?

*Terry:* Well, how do we know the clerks are ringing up all the merchandise?

*Lori:* That's one of the strong points about the system. The scanner automatically rings up each item, based on its bar code. We update the prices daily, so we're sure that the sale is rung up for the right price.

*Terry:* That's not my concern. What keeps a clerk from pretending to scan items and then simply not charging his friends? If his friends were buying 10-15 items, it would be easy for the clerk to pass through several items with his finger over the bar code or just pass the merchandise through the scanner with the wrong side showing. It would look normal for anyone observing. In the old days, we at least could hear the cash register ringing up each sale.

*Lori:* I see your point.

 Suggest ways that Yoder Brothers Grocery Stores could prevent or detect the theft of merchandise as described.

**SA 8-4**  
Ethics and professional conduct in business

Ryan Egan and Jack Moody are both cash register clerks for Organic Markets. Lee Sorrell is the store manager for Organic Markets. The following is an excerpt of a conversation between Ryan and Jack:

*Ryan:* Jack, how long have you been working for Organic Markets?

*Jack:* Almost five years this November. You just started two weeks ago . . . right?

*Ryan:* Yes. Do you mind if I ask you a question?

*Jack:* No, go ahead.

*Ryan:* What I want to know is, have they always had this rule that if your cash register is short at the end of the day, you have to make up the shortage out of your own pocket?

*Jack:* Yes, as long as I've been working here.

*Ryan:* Well, it's the pits. Last week I had to pay in almost \$40.


*Jack:* It's not that big a deal. I just make sure that I'm not short at the end of the day.

*Ryan:* How do you do that?

*Jack:* I just shortchange a few customers early in the day. There are a few jerks that deserve it anyway. Most of the time, their attention is elsewhere and they don't think to check their change.

*Ryan:* What happens if you're over at the end of the day?

*Jack:* Lee lets me keep it as long as it doesn't get to be too large. I've not been short in over a year. I usually clear about \$20 to \$30 extra per day.

 Discuss this case from the viewpoint of proper controls and professional behavior.

**SA 8-5**  
Bank reconciliation and internal control

The records of Anacker Company indicate a July 31 cash balance of \$9,400, which includes undeposited receipts for July 30 and 31. The cash balance on the bank statement as of July 31 is \$6,575. This balance includes a note of \$4,000 plus \$160 interest collected by the bank but not recorded in the journal. Checks outstanding on July 31 were as follows: No. 370, \$580; No. 379, \$615; No. 390, \$900; No. 1148, \$225; No. 1149, \$300; and No. 1151, \$750.


On July 3, the cashier resigned, effective at the end of the month. Before leaving on July 31, the cashier prepared the following bank reconciliation:

Cash balance per books, July 31 . . . . .		\$ 9,400
Add outstanding checks:		
No. 1148 . . . . .	\$225	
1149 . . . . .	300	
1151 . . . . .	750	1,175
		<u>10,575</u>
Less undeposited receipts . . . . .		4,000
Cash balance per bank, July 31 . . . . .		\$ 6,575
Deduct unrecorded note with interest . . . . .		4,160
True cash, July 31 . . . . .		<u>\$ 2,415</u>

*Calculator Tape of Outstanding Checks:*

0 \*  
 225 +  
 300 +  
 750 +  
 1,175 \*

Subsequently, the owner of Anacker Company discovered that the cashier had stolen an unknown amount of undeposited receipts, leaving only \$1,000 to be deposited on July 31. The owner, a close family friend, has asked your help in determining the amount that the former cashier has stolen.

1. Determine the amount the cashier stole from Anacker Company. Show your computations in good form.
2. How did the cashier attempt to conceal the theft?
3. a. Identify two major weaknesses in internal controls, which allowed the cashier to steal the undeposited cash receipts.  
 b.  Recommend improvements in internal controls, so that similar types of thefts of undeposited cash receipts can be prevented.

**SA 8-6**  
 Observe internal  
 controls over cash

**Group Project**

Select a business in your community and observe its internal controls over cash receipts and cash payments. The business could be a bank or a bookstore, restaurant, department store, or other retailer. In groups of three or four, identify and discuss the similarities and differences in each business's cash internal controls.


**SA 8-7**  
 Cash to monthly  
 cash expenses ratio



**OccuLogix, Inc.**, provides treatments for eye diseases, including age-related macular degeneration (AMD). The company's treatment system, called the RHEO system, consists of an Octonova pump and disposable treatment sets that improve microcirculation in the eye by filtering high molecular weight proteins and other macromolecules from the patient's plasma. OccuLogix reported the following data (in thousands) for the years ending December 31, 2006, 2005, 2004, and 2003:

	2006	2005	2004	2003
Cash as of December 31*	\$15,536	\$41,268	\$60,040	\$1,239
Net cash flows from operating activities	(14,548)	(18,710)	(5,382)	(2,375)

\*Includes cash equivalents and short-term investments.

1. Determine the monthly cash expenses for 2006, 2005, 2004, and 2003. Round to one decimal place.
2. Determine the ratio of cash to monthly expenses as of December 31, 2006, 2005, 2004, and 2003. Round to one decimal place.
3.  Based on (1) and (2), comment on OccuLogix's ratio of cash to monthly operating expenses for 2006, 2005, 2004, and 2003.