Cash and Internal Control

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Textbook: Financial Accounting, Spiceland

- This presentation contains information, in addition to the material prepared and provided by the professor, from the book Financial Accounting, 4th. Ed., Spiceland which is the textbook assigned for the course CONT 3105 – "Introducción a los Fundamentos de Contabilidad" at the University of Puerto Rico, Río Piedras Campus.

Topics

Topics

1.0 Fraud
2.0 Internal Control
3.0 Cash
4.0 Cash Controls
5.0 Recording Cash Transactions
6.0 Bank Reconciliation

Fraud

Fraud

1.1 Introduction

Fraud

1.1 Introduction

- According to research conducted by the Association of Certified Fraud Examiners, U.S. organizations lose an estimated $1 trillion (or about 5% of their total revenue) to employee fraud each year. This occurs despite increased corporate emphasis on antifraud controls and recent legislation to combat fraud.

Fraud

1.1 Introduction

- While some employees seat office supplies, inventory, and equipment, the asset most often targeted is cash.
- Cash fraud includes skimming cash receipts before they are recorded, stealing cash that has already been recorded, and falsely disbursing cash through fraudulent billing, expense reimbursement, or payroll.

Fraud

1.1 Introduction

- Consequently, we will discuss in this presentation other aspect about fraud, specially those related to cash.
- In addition, we will discuss internal controls to protect cash.

Fraud

1.2 Incorrect Financial Statements

Fraud

1.2 Incorrect Financial Statements

- Companies issue incorrect financial statements for two reasons:
  1. Errors
  2. Fraud

Fraud

1.2 <u>Incorrect Financial Statements</u>

1. **Errors**: Companies sometimes make accidental errors in recording (or failing to record) transactions or in applying accounting rules. When these errors are later discovered, companies often have to restate the financial statements affected, Even though these errors may be unintentional, they nevertheless can create confusion and weaken investors' and creditors' confidence in the important information role that accounting serves.

Fraud

1.2 Incorrect Financial Statements

2. **Fraud**: Fraud occurs when a person intentionally deceives another person for personal gain or to damage that person. Specifically related to business activities, the Association of Certified Fraud Examiners defines occupational fraud as the use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employer's resources.

Fraud

1.2 Incorrect Financial Statements

2. **Fraud**:
   a. **Misuse of Company Resources**: Occupational fraud is a big business, with company expecting to lose on average 5% of total revenues to fraud each year. Cash is the asset most commonly involved with fraudulent activity. Therefore, we will discuss the procedures businesses use to maintain control over cash receipts and cash disbursements.

Fraud

1.2 Incorrect Financial Statements

2. **Fraud**:
   b. **Financial Statement Manipulation**: The manipulation occurs when those in charge for communicating financial accounting information falsify reports (“cooking the books”). Some managers are willing to cook the books for personal gain. Motives for such deception might be maximizing their compensation, increasing the company’s stock price, and preserving their jobs.

Fraud

1.2 Incorrect Financial Statements

2. **Fraud**:

   b. **Financial Statement Manipulation**: Two of the highest-profile cases of accounting fraud in U.S. history are the collapses of Enron and WorldCom. Enron used questionable accounting practices to avoid reporting billions in debt and losses in its financial statements. WorldCom misclassified certain expenditures into overvaluing the company's stock.

Fraud

1.2 Incorrect Financial Statements

2. Fraud:

- **b. Financial Statement Manipulation**: As the Enron and WorldCom frauds were being uncovered in 2001 and 2002, the stock prices of these companies plummeted. Investors lost nearly $200 billion as a result. Employees of these companies also suffered. Both firms declared bankruptcy, resulting in employee termination, loss of employee retirement funds, stock options, and health benefits.

Fraud

1.3 Sarbanes-Oxley Act of 2002

Fraud

1.3 Sarbanes-Oxley Act of 2002

- In response to these corporate accounting scandals, Congress passed the Sarbanes-Oxley Act, also known as the Public Company Accounting Reform and Investor Protection Act of 2002 (SOX).

Fraud

1.3 Sarbanes-Oxley Act of 2002

- SOX applies to all companies that are required to file financial statements with the SEC and represents once of the greatest reforms in business practices in U.S. history. The act established a variety of guidelines related to auditor-client relations and internal control procedures.

Fraud

1.4 Fraud Triangle

Fraud

1.4 Fraud Triangle

- The three elements necessary for every fraud are commonly referred to as the fraud triangle, and they are:
  1. **Opportunity**: The situation allows the fraud to occur.
  2. **Motivation**: Someone feels the need to commit fraud, such as the need for money.
  3. **Rationalization**: Justification for the deceptive act by the one committing the fraud.

Fraud

1.4 Fraud Triangle

- To minimize fraud, at least one of the three elements of the fraud triangle must be eliminated. Of the three elements, companies have the greatest ability to eliminate the opportunity.
- To eliminate opportunity, companies implement formal procedures known as internal controls.

Internal Control

Internal Control

2.1 Definition

Internal Control

2.1 Definition

- Internal controls is a company's plan to:
  1. Safeguard the company's assets, and
  2. Improve the accuracy and reliability of accounting information.
- Effective internal control builds a wall to prevent misuse of company funds by employees and fraudulent or errant financial reporting. Strong internal control systems allow greater reliance by investors or reported financial statements.

Internal Control

2.2 Components of Internal Control

Internal Control

2.2 <u>Components of Internal Control</u>

- The components of internal control are:
  1. Control Environment
  2. Risk Assessment
  3. Control Activities
  4. Monitoring

Internal Control

2.2 Components of Internal Control

1. **Control Environment**: The control environment sets the overall ethical tone of the company with respect to internal control. It includes formal policies related to management's philosophy, assignment of responsibilities, and organizational structure.

Internal Control

2.2 Components of Internal Control

2. **Risk Assessment**: Identifies and analyzes internal and external risk factors that could prevent a company's objective from being achieved.
   - *Internal Factors:* Some internal factors could be unsafe lighting, employees without proper supervision, free access to inventory warehouse, and employee incompetence with regard to providing services.

Internal Control

2.2 Components of Internal Control

2. **Risk Assessment**:
   - *External Factors:* Vendor supplying low-quality inventory, decline in customer demand, among others.

Internal Control

2.2 Components of Internal Control

3. **Control Activities**: Control activities includes a variety of policies and procedures used to protect a company's assets. There are two general types of control activities: preventive and detective. Preventive controls are designed to keep errors or fraud from occurring in the first place. Detective controls are designed to detect errors or fraud that already have occurred.

Internal Control

2.2 Components of Internal Control

3. **Control Activities**:
   a. Preventive controls: Example of preventive controls includes:
      i. *Separation of duties*: A set of procedures intended to separate duties among employees for authorizing transactions, recording transactions, and controlling related assets. **Example**: one employee authorizes a payment, another employee signs the check and a third employee records the transaction on the books.

Internal Control

2.2 Components of Internal Control

3. Control Activities:

a. Preventive controls: Example of preventive controls includes:

ii. *Physical Controls*: Proper physical control over assets and accounting records. **Example**: custody of cash collected; electronic records backup daily, etc.

iii. *Proper Authorization*: Formal guidelines on how to use company's resources and authorize transactions, such as purchase of supplies or services or issuing a check.

Internal Control

2.2 Components of Internal Control

3. Control Activities:

a. Preventive controls: Example of preventive controls includes:

iv. *Employee Management*: Provide employees with appropriate guidance to ensure they have the knowledge necessary to carry out their job duties.

Internal Control

2.2 Components of Internal Control

3. Control Activities:

a. Preventive controls: Example of preventive controls includes:

v. *E-commerce Controls*: E-commerce refers to a wide range of electronic activities of a company, such as buying and selling over the Internet, digital information processing, and electronic communication. Internal controls include: passwords to conduct electronic business transactions, check the firewall settings, update antivirus software, etc.

Internal Control

2.2 Components of Internal Control

3. Control Activities:

b. Detective controls: Examples of Detective Controls include:

i. *Reconciliation*: Management should periodically determine whether the amount of physical assets of the company, such as cash or inventory, agree with the accounting records.

Internal Control

2.2 Components of Internal Control

3. Control Activities:

b. Detective controls: Examples of Detective Controls include:

ii. *Performance Reviews*: The actual performance of individuals or processes should be checked against their expected performance. For example: Sales are lower than expected, employees could be stealing inventory or the vendors are supplying low-quality product.

Internal Control

2.2 Components of Internal Control

3. **Control Activities**:
   b. Detective controls: Examples of Detective Controls include:
      ii. *Audit*: Many companies, such as those companies listed on stock exchange, are required to have an independent auditor attest to the adequacy of their internal control procedures.

Internal Control

2.2 Components of Internal Control

4. **Monitoring**: Continual monitoring of internal activities and reporting of deficiencies is required. Monitoring includes formal procedures for reporting control deficiencies.

Internal Control

2.3 Responsibilities for Internal Control

Internal Control

2.3 Responsibilities for Internal Control

- Everyone in a company has an impact on the operation and effectiveness of internal controls, but the top executives are the ones who must take final responsibility for their establishment and success.

Internal Control

2.4 Limitations of Internal Control

Internal Control

2.4 Limitations of Internal Control

- No internal control is perfect. While better internal control systems will more likely detect operating and reporting errors, no internal control system can turn a bad employee into a good one.

Internal Control

2.4 Limitations of Internal Control

- Internal control systems are especially susceptible to collusion. Collusion occurs when two or more people act in coordination to circumvent internal control.
- Fraud cases that involve collusion are typically several times more severe than are fraud cases involving one person.

Cash

Cash

3.1 Definition

Cash

3.1 Definition

- The amount of cash recorded in a company's balance sheet includes:
  1. Currency and coins.
  2. Checks received.
  3. Balances in savings and checking accounts.
  4. Credit card and debit card sales.
  5. Cash equivalents.

Cash

3.2 Cash Equivalent

Cash

3.2 Cash Equivalent

- Cash equivalents are defined as short-term investments that have a maturity date no longer than three months from the date of the purchase.
- **Examples**:
    1. Money market funds.
    2. Treasury bills
    3. Certificate of deposits.

Cash Controls

Cash Controls

4.1 Controls Over Cash Receipts

Cash Controls

4.1 Controls Over Cash Receipts

- Most businesses receive payment from the sale of products and services either in the form of cash or as a check received immediately or through the mail.
- Common controls over cash receipts follows.

Cash Controls

4.1 Controls Over Cash Receipts

1. **Customer Checks**: Open mail each day, and make a list of checks received, including the amount and payer's name.

Cash Controls

4.1 Controls Over Cash Receipts

2. **Credits Cards**: Accept credit cards or debit cards, to limit the amount of cash employees handle.

Cash Controls

4.1 Controls Over Cash Receipts

3. **Immediate Deposit**: Designate an employee to deposit cash and checks into the company's bank account each day, different from the person who receives cash and checks.

Cash Controls

4.1 Controls Over Cash Receipts

4. **Recording:** Have another employee record cash receipts in the accounting records as soon as possible. Verify cash receipts by comparing the bank deposits slip with the accounting records.

Cash Controls

4.2 Controls Over Cash Disbursements

Cash Controls

4.2 Controls Over Cash Disbursements

- Managers should design proper controls for cash disbursements to prevent any unauthorized payments and ensure proper recording.
- Cash disbursements include not only disbursing physical cash, but also
  1. writing checks,
  2. using credit cards and debit cards, and
  3. electronic cash transfers.

Cash Controls

4.2 Controls Over Cash Disbursements

- Common controls over cash disbursements include:
  1. **Method of Payment**: Make all disbursements, other than very small ones, by check, debt card, or credit card. This provide permanent record of all disbursements.
  2. **Authorization**: Authorize all expenditure before purchase. The employee who authorizes payment should not also be the employee who prepares the check.
  3. **Serial Numbered Checks**: Make sure checks are serially numbered and signed only by authorized employees. Requires two signatures for larger checks.

Cash Controls

4.2 Controls Over Cash Disbursements

- Common controls over cash disbursements include:

4. **Purchase Limits**: Set maximum purchase limits on debit cards and credit cards. Give approval to purchase above these amounts only to upper-level employees.
5. **Segregation of Duties**: Employees responsible for making cash disbursement should not also be in charge in cash receipts.
6. **Review of Invoice**: Periodically agree amounts shown in the debit card or credit card statements against purchase receipts. The employee verifying the accuracy of the debit card and credit card statements should not also be the employee responsible for actual purchases.

Recording Cash Transactions

Recording Cash Transactions

5.1 Cash Receipts

Recording Cash Transactions

5.1 Cash Receipts

1. **Acceptance of Customers Checks**: When a customer uses cash or a check to make a purchase, the company records the transactions as a cash sale.

Recording Cash Transactions

5.1 Cash Receipts

1. **Acceptance of Customers Checks**:

- **Example**: As of 4/15/2018 the Company provided services amounting $5,000. The clients paid $1,500 in cash and $3,500 in checks.

GENERAL JOURNAL				
Date	**Account Title**	**Ref.**	**Debit**	**Credit**
Apr. 15	Cash		5,000	
	Service Revenue			5,000
	(*Record revenues and receive cash or checks.*)			

Recording Cash Transactions

5.1 Cash Receipts

2. **Acceptance of Credit Cards**: The term credit card is derived from the fact that the issuer, such a VISA or MasterCard, extends credit (lends money) to the cardholder each time the cardholder uses the card. Meanwhile, the credit card company deposits cash in the company's bank for the amount of the sales, less service fees.

Recording Cash Transactions

5.1 Cash Receipts

2. **Acceptance of Credit Cards**: Credit card companies charge the retailer, not the customer, for the use of the credit card. This is the service fees. This charge generally ranges from 2% to 4% of the amount of the sale.

Recording Cash Transactions

5.1 Cash Receipts

2. Acceptance of Credit Cards:

- **Example**: As of 4/15/2018 the Company provided services amounting $5,000 and the clients paid using credit cards. The credit card company service charge is a 3% [or $150 ($5,000 x 3%)].

GENERAL JOURNAL				
Date	**Account Title**	**Ref.**	**Debit**	**Credit**
Apr. 15	Cash		4,850	
	Service Fees Expense		150	
	Service Revenue			5,000
	(*Record revenues with credit card, 3% fees.*)			

Recording Cash Transactions

5.1 Cash Receipts

3. **Acceptance of Debit Cards**: Like credit cards, debit cards offer customers a way to purchase goods and services without a physical exchange of cash. They differ, however, in that most debt cards work just like a check and withdraw funds directly from the cardholder's bank account at the time of use.

Recording Cash Transactions

5.1 Cash Receipts

3. **Acceptance of Debit Cards**: Similar to credit cars, the use of debit cards by customers results in a fee being charged to the retailer. However, the fees charged for debit cards are typically much lower than those charged for credit cards. Debit card transactions are recorded similar to credit card transactions.

Recording Cash Transactions

5.2 Cash Disbursement

Recording Cash Transactions

5.2 Cash Disbursement

1. **Payment Using Cash, Checks or Debit Cards**: When a company use cash, checks or debit cards to make purchases, the cash account is reduced immediately. Consequently, when the transaction is recorded on books, the company credit the cash account.

Recording Cash Transactions

5.2 <u>Cash Disbursement</u>

1. **Payment Using Cash, Checks or Debit Cards**:
   - **Example**: As of 4/15/2018 the Company paid $3,500 using a <u>check</u> for repairing the air conditioning system of the premises.

GENERAL JOURNAL				
Date	**Account Title**	**Ref.**	**Debit**	**Credit**
Apr. 15	Repair Expense		3,500	
	Cash			3,500
	(*Record repair of air conditioning system.*)			

Recording Cash Transactions

5.2 Cash Disbursement

2. **Payment Using Credit Cards**: Because credit cards allow the purchaser to delay payment for several weeks or even months, if a company use credit cards to make purchases, a liability is recorded.

Recording Cash Transactions

5.2 Cash Disbursement

2. **Payment Using Credit Card**:

- **Example**: As of 4/15/2018 the Company paid $3,500 using a credit card for repairing the air conditioning system of the premises.

GENERAL JOURNAL				
Date	**Account Title**	**Ref.**	**Debit**	**Credit**
Apr. 15	Repair Expense		3,500	
	Accounts Payable			3,500
	(*Record repair of air conditioning system.*)			

Bank Reconciliation

Bank Reconciliation

6.1 Definition

- A bank reconciliation matches the balance of cash in the bank account with the balance of cash in the company's own records.

Bank Reconciliation

6.2 Purpose

Bank Reconciliation

6.2 Purpose

- A company's cash balance as recorded in its books rarely equals the cash balance reported in the bank statement. That is the reason why the company needs to prepare a bank reconciliation, to reconcile the differences between the cash balance on the bank and the cash balance on company's books.

Bank Reconciliation

6.2 Purpose

- Some reasons for the differences are:

1. The company has cash receipts that have not yet been deposited on the bank.
2. The company have written a check that has not been paid by the bank.
3. The bank make a recording error.

Bank Reconciliation

6.3 Classification of Differences

Bank Reconciliation

6.3 Classification of Differences

- The differences are classified as

1. **Timing differences**: Occur when the company records transactions either before or after the bank records the same transactions.
   - **Example**: On April 30, 2018, the company paid a supplier $1,000 by check. Immediately, the company recorded the transaction on the books decreasing the cash balance. However, the supplier cashed the check on May 2, 2018. Consequently, the balance of cash in the company' s records will be reduced a couple of days earlier than will the bank's.

Bank Reconciliation

6.3 Classification of Differences

- The differences are classified as

2. **Errors**: Errors can be made either by the company or its bank and may be accidentally or intentional. An accidental error might occur if the company mistakenly were to record a check being written for \$117 as \$171 in its records, or if the bank improperly processed a deposit of \$1,100 as a \$1,010 deposit.

Bank Reconciliation

6.3 Classification of Differences

- The differences are classified as

2. **Errors**: An intentional error is the result of theft. If the company records a daily deposit of $5,000 but an employee deposits only $500 into the bank account and pockets the rest, the bank reconciliation will reveal the missing $4,500.

Bank Reconciliation

6.4 Steps to Reconcile a Bank Account

Bank Reconciliation

6.4 Steps to Reconcile a Bank Account

- Reconciling the bank account involves three steps:

1. Reconcile the bank's cash balance.
2. Reconcile the company's cash balance.
3. Update the company's cash account by recording items identified in Step 2.

- *Each step is explained using the Comprehensive Example on next page.*

Comprehensive Example – Bank Reconciliation

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

- Vienna School Corporation has one cash account in Local Bank. In order to reconcile this cash account, as of April 30, 2018 we need to review the following documents or information:
    1. Cash receipts of the company during April 2018.
    2. Cash disbursement of the company during April 2018.
    3. Cash balance in General Ledger as of April 30, 2018.
    4. Bank Statement of Local Bank of April 2018.

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

- The Cash Receipts of the Vienna School during April 2018 are:

VIENNA SCHOOL – CASH RECEIPTS		
Date	**Deposit**	**Amount**
April 07, 2018	Sales receipts.	$5,000
April 21, 2018	Sales receipts.	2,750
April 27, 2018	Sales – check received	1,000
April 30, 2018	Sales receipts	3,100
	Total Deposits	**$11,850**

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

- The Cash Disbursements of the Vienna School during April 2018 are:

VIENNA SCHOOL – CASH DISBURSEMENTS		
Date	**Check**	**Amount**
April 02, 2018	Check 207	$1,000
April 12, 2018	Check 208	500
April 13, 2018	Check 209	1,030
April 17, 2018	Check 210	2,500
April 27, 2018	Check 211	830
	Total Payments	**$5,860**

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

- The Cash Balance of the Vienna School as of April 30, 2018 is:

VIENNA SCHOOL – CASH BALANCNE	
Date	**Amount**
Beginning Balance, April 1	$7,100
+ Deposits	11,850
- Checks	5,860
Ending Balance, April 30	**$13,090**

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

- The Bank Statement of Local Bank of April 30, 2018 is presented on next page.

Bank Reconciliation

LOCAL BANK			
VIENNA SCHOOL CORPORATION **Main Street , #100, TX, 79760**		**Account Number: 081-353535** **Statament: April 30, 2018**	
Beg. Bal. $ 7,100	Deposits/Credits $11,765	Withdrawals/Debits $3,835	End. Bal. $15,030
Deposits/Credits		**Withdrawals/Debits**	
4/7	$5,000	4/2 – Ck. 207	$1,000
4/21	2,750	4/12 – Ck. 208	500
4/23 Client electronic transfer-accounts receivable	3,000	4/13 – Ck. 209	1,300
4/27	1,000	4/29 Deposit return	1,000
4/30 Interest earned	15	4/30 Bank charges	35
	$11,765		$3,835

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

1. **Reconcile the <u>bank's cash balance</u>**: First, we consider cash transactions recorded by the company, but not yet recorded by its bank. These include:
   a. **Deposits Outstanding**: Cash receipts of the company that have not been added to the bank's record of the company's balance.
   b. **Checks Outstanding**: Checks the company has written that have not been subtracted from the bank's record of the company's balance.

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

- The <u>Cash Receipts</u> of the Vienna School during April 2018 are:

VIENNA SCHOOL – CASH RECEIPTS		
Date	**Deposit**	**Amount**
April 07, 2018	Sales receipts.	$5,000
April 21, 2018	Sales receipts.	2,750
April 27, 2018	Sales – check received	1,000
April 30, 2018	Sales receipts	3,100
	Total Deposits	**$11,850**

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

- The <u>Cash Disbursements</u> of the Vienna School during April 2018 are:

VIENNA SCHOOL – CASH DISBURSEMENTS		
Date	**Check**	**Amount**
April 02, 2018	Check 207	$1,000
April 12, 2018	Check 208	500
April 13, 2018	Check 209 (Rent Expense)	1,030
April 17, 2018	Check 210	2,500
April 27, 2018	Check 211	830
	Total Payments	**$5,860**

Bank Reconciliation

LOCAL BANK			
VIENNA SCHOOL CORPORATION **Main Street , #100, TX, 79760**		**Account Number: 081-353535** **Statament: April 30, 2018**	
<u>Beg. Bal.</u> $ 7,100	<u>Deposits/Credits</u> $11,765	<u>Withdrawals/Debits</u> $3,835	<u>End. Bal.</u> $15,030
Deposits/Credits		**Withdrawals/Debits**	
4/7	$5,000	4/2 – Ck. 207	$1,000
4/21	2,750	4/12 – Ck. 208	500
4/23 Client electronic transfer-accounts receivable	3,000	4/13 – Ck. 209	1,300
4/27	1,000	4/29 NSF	1,000
4/30 Interest earned	15	4/30 Bank charges	35
	$11,765		$3,835

Bank Reconciliation

VIENNA SCHOOL CORPORATION **Bank Reconciliation** **April 30, 2018**			
Bank's Cash Balance		**Company's Cash Balance**	
Per Bank Statement	$15,030	Per General Ledger	$13,090
+ Deposit outstanding 4/30	3,100		
- Checks outstanding #210 $2,500 #211 $ 830	(3,330)		
	$14,800		

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

2. **Reconcile the company's cash balance**: Next, we need to reconcile the company's cash balance. Here are some common items that will increase the company's cash balance once the reconciliation occurs:
   a. **Bank Collections**: Collections on the company's behalf, such as payment from customers, real estate transactions, collection agencies, and lending arrangement.

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

2. **Reconcile the <u>company's cash balance</u>**:
   b. **Interests**: Earn interest on saving or checking accounts.
   c. **NSF Checks**: The company receives a customer's check and deposits that check, recording an increase in cash. However, the company later finds out from the bank statement that the customer's check was bad, and the company needs to decrease its cash balance to undo the initial increase.

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

2. **Reconcile the company's cash balance**:
   - d. **Debits Charge**: Purchased made by company's employees. These purchases are immediately withdrawn from the bank account, but they may not be known by the company's accountant until examination of the bank statement.
   - e. **Electronic Funds Transfers**: Payment of mortgage or utilities by automatic payments.
   - f. **Services fees**: ATM use, wire transfers, monthly fees, foreign currency exchange, etc.

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

2. **Reconcile the company's cash balance**:

- In **conclusion**, you must review the bank statement and identify those items in the statements that are not included on company's books including errors recorded on company's books identified in the bank statements.
- Let's see the Local Bank statement on the page to identify those items.

Bank Reconciliation

LOCAL BANK			
VIENNA SCHOOL CORPORATION **Main Street , #100, TX, 79760**		**Account Number: 081-353535** **Statament: April 30, 2018**	
Beg. Bal. $ 7,100	Deposits/Credits $11,765	Withdrawals/Debits $3,835	End. Bal. $15,030
Deposits/Credits		**Withdrawals/Debits**	
4/7	$5,000	4/2 – Ck. 207	$1,000
4/21	2,750	4/12 – Ck. 208	500
4/23 Client electronic transfer-accounts receivable	3,000	4/13 – Ck. 209	1,300
4/27	1,000	4/29 NSF	1,000
4/30 Interest earned	15	4/30 Bank charges	35
	$11,765		$3,835

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

2. **Reconcile the <u>company's cash balance</u>:**

- Pay attention to the following amounts included on the bank statement, but not in the company's books:
  1. Client electronic transfer: $3,000.
  2. Interest income: $15.
  3. Error on Ck. 209 of $270 ($1,300 - $1,030).
  4. NSF: $1,000.
  5. Bank charges: $35.
- This amount must be included on bank reconciliation below Company's Cash Balance section. See next page.

Bank Reconciliation

VIENNA SCHOOL CORPORATION **Bank Reconciliation** **April 30, 2018**			
Bank's Cash Balance		**Company's Cash Balance**	
Per Bank Statement	$15,030	Per General Ledger	$13,090
+ Deposit outstanding 4/30	3,100	+ Collection from client	3,000
- Checks outstanding #210 $2,500 #211 $ 830	(3,330)	+ Interest earned	15
		- Correct amount #209 ($1,300)	270
		- NSF	1,000
		- Bank Charges	35
Bank Balance per Reconciliation	**$14,800**	**Company Balance per Reconciliation**	**$14,800**

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

3. **Update the company's Cash account by recording items identified in Step 2**: As a final step in the reconciliation process, a company must update the balance in its cash account, to adjust for the items used to reconcile the company's cash balance. Consequently, the five (5) items used in the bank reconciliation to reconcile the company's cash balance recorded on books since those amount are not yet recorded on company's records.

Bank Reconciliation

Comprehensive Example – Bank Reconciliation

3. **Update the company's Cash account by <u>recording</u> items identified in Step 2**: Out of the five items, there are two items that increase the cash balance. The entry to record these items follows:

GENERAL JOURNAL				
Date	**Account Title**	**Ref.**	**Debit**	**Credit**
Apr. 30	Cash		3,015	
	Account Receivable			3,000
	Interest Income			15
	(*Record collection of A/R and interests.*)			

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

3. **Update the company's Cash account by <u>recording</u> items identified in Step 2**: Out of the five items, there are three items that decrease the cash balance. The entry to record these items follows:

GENERAL JOURNAL				
Date	**Account Title**	**Ref.**	**Debit**	**Credit**
Apr. 30	Bank Charge Expense		35	
	Account Receivable		1,000	
	Rent Expense		270	
	Cash			1,305
	(*Record collection of A/R and interests.*)			

Bank Reconciliation

<u>Comprehensive Example – Bank Reconciliation</u>

3. **Update the company's Cash account by <u>recording</u> items identified in Step 2**: When the two journal entries are posted to the Cash Account in the General Ledger, the cash balance is updated to present the reconciled balance as follows:

CASH

Bal. 30 abr.	$13,090	1,305
	<u>3,015</u>	
	<u>$14,800</u>	