

ST. MARY'S UNIVERSITY
BUSINESS FACULTY
DEPARTMENT OF ACCOUNTING

ASSESSMENT OF INTERNAL CONTROL OVER CASH
THE CASE OF NATIONAL ALCOHOL AND LIQUOR FACTORY

BY:

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SMUC

JUNE 2014

ADDIS ABABA

**ASSESSMENT OF INTERNAL CONTROL OVER CASH
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**A SENIOR RESEARCH SUBMITTED TO THE
DEPARTMENT OF ACCOUNTING
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**IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR
THE DEGREE OF BACHELOR OF ARTS IN ACCOUNTING**

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DECLARATION

Advisee's Declaration

We, the undersigned, declare that the senior essay is our original work, prepared under the guidance of Instructor Yeserash. All sources of materials used for the manuscript have been duly acknowledged.

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Advisor's declaration

The paper has been submitted for examination with my approval as the University College advisor.

Name: Instructor Yeserash

Signature: _____

Date: _____

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God bless you all in abundance!!

ABSTRACT

Internal control over cash is of major importance in any business enterprise since cash is a vital factor in the operation of business and many business transactions involve cash. In addition, controlling of cash is important since it is the most liquid of all assets that is vulnerable to theft or misappropriation.

Due to the execution and involvement of cash and its flow in different institutions, there might have been problems like mishandling and misuse of unreliable and unreal formats and documents as well as effectiveness with lack of proper timing and authority are among the problems.

This study will mainly focus on some of the controlling mechanisms that might have been overlooked on the internal control policies over cash in the case of National Alcohol and Liquor Factory and to give some valuable feedback to the management. To execute, our study uses primary data by interviewing the factory's stakeholders who are responsible members and review their cash operation manual guidelines and reports as well as different resources from the company's website.

CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

According to (Mosich: A.N 1989) Cash has always attracted auditors' attention for many good reasons. As it is the most liquid of all, transactions directly or indirectly affect the diverse nature of the process involved in billing, collections, deposits and disbursements. Implementing internal control in the area of cash management is very difficult. It is the asset most likely to be diverted and improperly used. Internal control was considered as a control measure taken by organizations to protect the assets of the factory from fraud, theft, and misappropriation by employees. The committee of sponsoring organization (COSO) report defines internal control as. "The process effected by an entity's board of directors, management and other personnel designed to provide reasonable assurance, regarding the achievement of objective like: reliability of financial reporting, compliance with applicable laws and regulations, and effectiveness and efficiency of operations.

The objective of internal control over cash is to make sure whether the organization is safeguarding and reporting cash in the appropriate manner as cash has the highest risk and is difficult to control.

The internal control process, which historically has been a mechanism for reducing instances of fraud, misappropriation and errors, has recently become more extensive, addressing all the various risks faced by organizations.

It is now recognized that a sound internal control process is critical to organization's ability to meet its established goals and objectives and maintain its financial ability. When properly designed and consistently enforced, a good system of internal control over cash will help management safeguard the organization's resources, produce reliable financial reports, and comply with laws and regulation. It will also reduce the possibility of significant errors and irregularities, as well as assist in their timely detection when they do occur.

1.2 Back Ground of the Organization

National Alcohol and Liquor Factory is a state owned business organization and pioneer factory in manufacturing and distributing pure Alcohol (C_2H_5OH), denatured Alcohol and different brands of liquor in the country. The factory comprises of three branches which were once established and owned by individuals in different periods. The branch factories are named as:- Sebeta branch factory/established in 1898 E.C. Akaki branch factory / established in 1930 E.C. Mekanissa branch factory / established in 1949 E.C. and the liquor section, previously called as Maichew Branch was established in 1906 E.C.

In 1949 E.C. the Ethiopian Government nationalized and owned the factories under the name of National Alcohol and Liquor Factory. The company has 546 employees, and it had been consistently mining a wealth experience in industrial production and marketing of pure Alcohol and variety of liquors. The company currently produces and distributes: - Pure alcohol with attained capacity of 1,814,206 liters/year; denatured alcohol with attained capacity of 133,169 liters/year and different brands of alcoholic drinks with attained capacity of 4,429,943 liters/year. Through our observations during the exploratory study, according to its business setting and its huge day to day cash transactions the factory needs extensive, tight and effective internal control procedures over cash but the student research team had identified some manifestations which led the team to raise questions about the strength and the convenience of the factory's internal control system over cash.

1.3 STATEMENT OF THE PROBLEM

As it is stated in the back ground part cash is the asset most likely to be diverted and improperly used so it needs effective internal control. Internal control is the process effected by an entity's board of directors, management and other personnel designed to provide reasonable assurance, regarding the achievement of providing reliable financial reports, Compliance with applicable laws and regulations and effective and efficient operations. Due to the above explanation a sound internal control over cash will help the management to safeguard organizational resources, produce reliable financial reports, and comply with laws and regulation formulated by itself or imposed by other external concerned bodies. It will also reduce the possibility of significant errors and irregularities, as well as assist in their timely detection when they do occur.

On the other hand if a firm has not such type sound internal control it may face the expected cash related risks like fraud and diverting to personal purpose.

This research is conducted by a student research team; the team had taken a preliminary study with in National alcohol and liquor factory of Ethiopia for the purpose of identifying the existence of researchable problem; and it identified the existence of cash related problems like cash shortage from daily cash sales and improper cash utilization. This firm is a manufacturing factory so most of its financial transactions are related with cash when it purchases inputs and sales outputs hence it needs strong internal control over cash; but the above problems are indicators for the factory's system of internal control over cash to be in question. Due to this the team was initiated and had planned to assess the strength and convenience of the factory's internal control (policies and procedures) over cash in order to identify the real causes of the existing problems and to suggest possible solutions for them.

In this paper, the research team based on its plan it has assessed the practice of internal control over cash in National Alcohol and Liquor Factory of Ethiopia and recommended some possible solutions for the identified causes of the research problem.

1.4 Research Questions

For solving the main research problem the real causes of the problem must be identified. Due to this based on the possible causes of the problem, the research team has raised and answered the following research questions.

1. What are the policies and procedures existing in the factory for executing cash payment transactions?
2. What are the policies and procedures existing in the factory for executing cash collection transactions?
3. To what extent is the factory's internal control over cash strong and convenient for the achievement of organizational goal?

1.5 OBJECTIVE OF THE STUDY

1.5.1 General Objective

The main objective of this study was to assess (examine) the strength and convenience of the Factory's internal control (policies and procedures) over cash in order to identify the real causes of the existing problems and to suggest possible solutions for them.

1.5.2 Specific Objectives

To achieve the above general objective, the research team planned the following specific objectives as specific activities for solving each research question.

1. To identify and evaluate the factory's policies and procedures exist on execution of cash payment transactions.
2. To identify and evaluate the factory's policies and procedures exist on execution of cash collection transactions.
3. To evaluate how much is the factory's internal control over cash strong and convenient to achieve the organizational goal.

1.6 SIGNIFICANCE OF THE STUDY

This paper clearly reflects most of the internal control practices over cash in National Alcohol and Liquor Factory and gives possible solution as to how financial manager should process potential healthy cash and undertake proper follow up measures when problems occur during cash collection and payments.

It might also be used as reference to those individuals who are interested to undertake further studies. It also recommends certain internal control procedures that make internal control effective.

1.7 DELIMITATION /SCOPE OF THE STUDY/

This research is delimited to only the cash control practice assessment on National Alcohol and Liquor Factory head office because the whole needed documents and data are available here so that the student research team did not need to include all branches. The study assessed only the current system of internal control over cash.

1.8 RESEARCH DESIGN AND METHODOLOGY

1.8.1. Research Design

As it was planned this research is conducted by applying both descriptive and explanatory research designs. Due to this, the major part of the whole collected data is related with the existing facts over cash control practice in National Alcohol and Liquor factory; and such facts are already described in chapter three of this paper by using frequency and percentage distributions of data analyses. The rest are explanations and reasoning of facts; this also explained in words in chapter three.

1.8.2. Sources and types of data

The research team has got the needed data from both primary and secondary sources. The primary data are obtained from the target study objects that means the factory's finance staff members, internal auditors and the general manager; and from the actual current practice of the firm. Secondary data are taken from the factory's financial audit report, procedural manuals, guidelines and regulations of financial activity.

1.8.3. Population and sampling design

The target population is as it is stated in the above section consists only the factory's finance staff members, internal auditor and general manager. The total population size is only 7 individuals; it is too small so that the whole population elements were taken as participants of the study.

1.8.4. Data Collection Methods

The student research team has collected the needed data from both primary and secondary data sources. For primary data, the team prepared questionnaire which consists many close ended questions and some open ended questions. 7 copies of the questionnaire were distributed and only 6 copies returned with responses. In addition to this the student research team members have observed the actual practice of the factory.

For the secondary data case the team has compiled the necessary data from the factory's financial audit report, procedural manuals, guidelines and regulations of financial activity.

1.8.5 Data Analysis Methods

This study used descriptive statistics for describing only the frequency and percentage distributions of respondents' response for each response alternative of the close ended questions. The collected data are ordered according to the type of questions and categorized based on the type of measurement scale they used. Such categorized data are presented in the form of table to describe the frequency and percentage distributions of responses easily. The tabulated data of each close ended question and the open ended questions' responses together with the observed primary data and secondary data are described and explained in words under each table.

1.9 LIMITATION OF THE STUDY

Even if the research was carefully designed and planned because of certain constraints like: time, lack of cooperativeness of respondents, finance problems and lack of experience, the research result is not that much deep and comprehensive as expected.

1.10 ORGANIZATION OF THE STUDY REPORT PAPER

The report paper has been classified in to four main chapters. The first chapter is the introduction part; it introduces about background of the study, statement of the research problem, research questions, objective of the study, significance of the study, research methodology, scope and limitation of the study and organization of the paper. Chapter two discusses the reviewed related and relevant literatures. Chapter three presents and discusses the collected empirical data by using the relevant method of data analysis. This chapter also interprets the result of the analyses and identify findings by comparing the result with its and other professional guide lines. Chapter four which is the last chapter, it summarizes the study findings, concludes the study and provides recommendations for findings which have negative influence on the cash control practice of the factory based on the known guidelines stated in chapter two.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.1 Definition of Cash

Cash is a medium of exchange that a bank will accept for deposit and immediate credit to the depositor's account cash includes paper currency and coin, personal checks, bank drafts, money orders, credit card sales drafts, and cashiers' checks as well as money on deposit with banks. (Mesich A.N. 1989)

Cash is needed to pay for labor and raw materials, to buy fixed assets, to pay taxes, to referred to as the "life blood of business enterprises" (Ross et al. 1998).

Cash is a current asset on deposit in a bank that can be withdrawn immediately and used for any business purpose, or cash is current asset that a bank will readily accept for deposit. Cash does not include postage stamps, bonds, promissory notes, postdated checks and certificates of deposit. They are not available for payment of current liabilities and immediate withdrawal. Cash is an asset that can be used to acquire goods and service.

2.2 Cash management

Cash management refers to planning, controlling and accounting for cash transactions and cash balances. It is the management of all financial resources. Cash management is major importance in any business enterprise because cash is a means of acquiring goods and services. Generally, cash management is centered on forecasting and internal controls. The responsibilities of management with respect to cash are:-

1. To assure that sufficient cash to carry on the operations.
2. To invest any idle cash.
3. To prevent loss of cash due to theft or misappropriation (Mesich–A.N. 1989)

2.3 Internal Control over Cash

It is necessary to safeguard cash effectively because of the ease with which it can be transferred. One of the major devices for maintaining control over cash is the being account. To obtain the most benefit from a bank account, all cash received must be deposited in the bank and all payments must be made by checks drawn on the work or from special cash funds.

Periodically, the bank mails to the depositor a statement of account. This statement of account should be reconciled with the depositor's records by preparation bank reconciliation. The bank reconciliation is divided into two major sections one section begins with the balance according to the bank statement and ends with an adjusted balance; the other section begins with the balance according to the depositor's records and also ends with an adjusted balance. After all reconciling items have been considered, the two amounts designated as the adjusted balance must be compared, the two amounts designated as the adjusted balance must be on.

After bank reconciliation has been prepared, the items which appear in the section of the bank reconciliation beginning with the balance according to the depositor's records must be entered into the accounting records through the use of adjusting journal entries.

1. To protect cash and ensure the accuracy of the accounting records for cash are effective internal control over cash is necessary.
2. Internal control system consists of organization plans, methods, and measures taken to safeguard assets from theft and unauthorized use. It ensures the accuracy and reliability of accounting records by intentional and unintentional in the accounting process. Effective internal control is achieved by proper segregation of duties and physical safeguards.
3. That is no one person or department is assigned to carry out all phases of a transaction and physical safeguards are used such as computers, cash registers and pre-numbered source documents.

2.4 Definition of Internal Control

Internal control means different things to different people. This causes confusion among business people, Legislators, Regulators and others, resulting in miscommunication and different perceptions. Problems are compounded when the term is not clearly defined, written in law, regulation or rule.

According to (Brigham,1995:356) internal control is important to: establish a common definition serving the needs of different parties.

Provide a standard against which business and other entities... large or small, in the public or private sector, for profit or not... can assess their control systems and determine how to improve the internal control. According to him, internal control is broadly defined as a process, affected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations.
- Reliability of financial reporting
- Compliance with applicable laws and regulations

The first category addresses an entity's basic business objectives including performance and profitability goals and safeguarding of resources. The second relates to the preparation of reliable published financial data derived from such statements, Such as earnings releases, Reported publicly. Third deals with complying with those laws and regulations to which the entity is subject. These distinct but overlapping categories address different needs and allow a directed focus to meet the separate needs.

Internal control systems operate at different levels of effectiveness. Internal control can be judged effective in each of the three categories, respectively, If the board of directors and management have reasonable assurance that:

- They understand the extent to which the entity's operates objectives is being achieved.
- Published financial statements are being prepared reliability.
- Applicable laws and regulations are being complied with.

While internal control is a process, its effectiveness is a state or condition of the process at one or more points in time.

2.5 Components of Internal Control

Internal control consists of five interrelated components. These are derived from the way an agreement runs a business, and are integrated with the management process. Although the components apply to all entities small and mid-size companies may implement them differently than large ones. Its controls may be less formal and less structured. Yet a small company can still have effective internal control. The components are:-

Control Environment: - the control environment sets the tone of an organization, influencing the control consciousness of its people it is the Foundation for all other components of internal control, Providing discipline and structure. Control environment factors include the integrity, ethical values and competence of the entity's people; management's philosophy and operating style: the way management assigns authority and responsibility and organizes and develops its people: and the attention and direction provide by the board of directors.

Risk Assessment: - every entity faces a variety of risks from external and internal sources that must be assessed. A precondition to risk assessment is establishment of objectives, linked at different levels and internally consistent. Risk assessment is the identification and analysis of relevant risks to achievement of the objectives, forming a basis for determining how the risks should be managed. Because economic, industry, regulatory and operating conditions will continue to change, mechanisms are needed to identify and deal with the special risks associated with change.

Control activities:- control activities are the policies and procedures that help ensure management directives are carried out. They help ensure that necessary actions are taken to address risks to achievement of the entity's objectives. Control activities occur throughout the organization, at all levels and in all functions. They include a range of activities as diverse as approvals, authorizations, verifications, and reconciliations, Review of operating performance, security of assets and segregation of duties.

Information and communication: - pertinent information must be identified, captured and communicated in a form and time frame that enable people to carry out their responsibilities. Information systems produce reports, containing operational, financial and compliance related information, that make it possible to run and control the business. They deal not only with internally generated data. But also information about external events activates and conditions necessary to informed business decision making and external reporting. Effective communication also must occur in a broader sense, flowing down, the across and up the organization. All personnel must receive a clear message form top management that control responsibilities must be taken seriously .They must understand their own role in the internal control system, as well as how individual activates relate to the work of others.

They must have a means of communicating significant information upstream. There also needs to be effective communication with external parties, such as customers, suppliers, regulators and share holders.

Monitoring: - internal control system needs to be monitored- a process that assesses the quality of the system's performance over time. This is accomplished through ongoing monitoring activities, separate evaluations or the combination of the two. Ongoing monitoring occurs in the course of operations. It includes regular management and supervisory activities, and other actions personnel take in performing their duties, the scope and frequency of separate evaluations will depend primarily on an assessment of risks and the effectiveness of ongoing monitoring procedures. Internal control deficiencies should be reported upstream. With serious matters reported to top management and the board.

There is synergy and linkage among these components, forming integrated systems that react dynamically to changing conditions. The internal control system is intertwined with the entity's operating activities and exists for fundamental business reasons. Internal control is most effective when controls are built in to the entity's infrastructure and are a part of the essence of the corporation. "Built in" controls support quality and empowerment initiatives, avoid unnecessary costs and enable quick response to changing conditions.

There is a direct relationship between the three categories of objectives, which are what an entity strives to achieve, and components, which represent what is needed to achieve the objectives. All components are relevant to each objectives category. The effectiveness and efficiency of operations is highly depend on all the five components of internal control over operation and functioning effectively to conclude that internal control over operations is effective.

The internal control definition with its underlying fundamental concepts of a process affected by people providing reasonable assurance together with the categorization of objectives; and the

components and criteria for effectiveness, and the associated discussions. (Constitute the internal control framework. James C.van Horne 2002)

2.6 Classification of Internal Control

Internal control is classified into two types, which are accounting and administrative controls.

Accounting Internal Control:- directly depends on the accounting records and financial statements. Administrative internal control heavily depends on the managerial aspects of control within the organization.

John w. cook and others in “**auditing philosophies and principles:**” book defines accounting controls consists of the methods, procedures and plans of organization that pertain mainly to protection of the assets and to assure that accounts and financial reports are reliable.

Administrative Internal Controls:- are procedures and methods that pertain primarily to the operation of corporation and managerial directives, Policies and reports. (Wongel, 2006)

2.7 Purpose of Internal Control

Managers (or owners) of small businesses often control the entire operation. They supervise workers, participate in all activities, and make major decisions. These managers usually purchase all of the business’s assets. They also hire and manage employees, negotiate all contracts, and sign all checks. These managers know from personal contact and observation whether the business is actually receiving the assets and services paid for larger companies cannot maintain this close personal supervision. They must delegate responsibilities and rely on formal procedures rather than personal contact in controlling business activities. An internal control system refers to the policies and procedures managers use to

- Protect assets.
- Ensure reliable accounting.
- Promote efficient operations.
- Urge adherence to company policies.

A Properly designed internal control system is a key part of systems design, analysis, and performance. Managers place a high priority on internal control systems because they can prevent avoidable losses. It helps managers plan operations, and monitor company and employee

performance while internal controls do not provide guarantees, the lower the company's risk of loss from not having internal controls. (Larson, 2002: 354)

2.8 Principle of Internal Control

Internal control policies and procedures vary from company to company they depend on factors such as the nature of the business and its size. Certain fundamental internal control principles apply to all companies, however.

The principles of internal control are to:

1. Establish responsibilities
2. Maintain adequate records.
3. Insure asset and bond key employees.
4. Separate record keeping from custody of assets.
5. Divide responsibility for related transactions.
6. Apply technological controls
7. Perform regular and independent reviews.

We explain these seven principles and describe how internal control procedures minimize the risk of fraud and theft. These procedures also increase the reliability and accuracy of accounting records.

A. Establish Responsibilities: Proper internal control means that responsibility for a task is clearly established and assigned to one person. When responsibility is not identified, determining who is at fault is difficult when a problem occurs. For instance, if two sales clerks share the same cash register, identifying which clerk is at fault if there is a cash shortage is difficult. Neither clerk can prove or disprove the alleged shortage. To prevent this problem, one clerk might be given responsibility for handling all cash sales.

B. Maintain Adequate Records: Good record keeping is part of an internal control system. It helps protect assets and ensures that employees use prescribed procedures. Reliable records are also a source of information that managers seek to monitor company activities. When detailed records of equipment are kept, For instance, Items are unlikely to be lost or stolen without detection.

- C. **Ensure Assets and Bond Key Employees**: good internal control means that assets are adequately insured against casualty and that employee handling cash and negotiable assets are bonded. An employee is bonded when a company purchases an insurance policy, or a bond, against losses from theft by that employee.
- D. **Separate Record Keeping from Custody of Assets**: an important principle of internal control is that a person who controls or has access to an asset must not keep that asset's accounting records. This principle reduces the risk of theft or waste of an asset because the person with control over it knows that another person keeps its records. Also a record keeper who does not have access to the asset has no reason to falsify records. This means that two people must both agree to commit a fraud, called collusion, to steal an asset and hide the theft from the records. Because collusion is necessary to commit this type of fraud, it is less likely to occur.
- E. **Divide Responsibility for Related Transactions**: good internal control divides responsibility for a transaction or a series of related transactions between two or more individuals or departments. This is to ensure that the work of one acts as a check on the other. This principle, often called separation of duties, is not a call for duplication of work. Each employee or department should perform unduplicated effort.
- F. **Apply Technological Controls**: cash registers, check protectors, time clocks, and personal identification scanners are examples of devices that can improve internal control. Technology often improves effectiveness of controls. Cash registers with a locked-in tape or electronic file make a record of each cash sale. A check protector perforates the amount of a check into its face and makes it difficult to alter the amount. A time clock registers the exact time an employee both arrives at and departs from the job—mechanical change and currency counters quickly and accurately count amounts, and personal scanners limit access to only authorized individuals. Each of these and other technological controls is an effective part of many internal control systems.
- G. **Perform Regular and Independent Reviews**: No internal control system is perfect. Changes in personnel and technological advances present opportunities for shortcuts and lapses. So does the stress of time presentation.

To counter these factors, regular review of internal control system is needed to ensure that procedures are followed. These reviews are preferably done by internal auditors not directly

involved in the activities. Their impartial prospective encourages an evaluation of the efficiency as well as the effectiveness of the internal control system. (Larson. 2002:354-65)

2.9 Internal Control and Computer

Computer processing of cash transactions can contribute to strong internal control over cash. Control over cash may be strengthened by the use of online register terminals. Remittance advices or mail room listings of customer's payments can be processed by computer. These days many companies use computers to issue checks and subsequently, to prepare bank reconciliations. The daily computer processing of cash receipts and checks can provide management with a continually up-to -date cash receipts journal, Check register, Customers' accounts ledger, and cash balance. In addition to this, the computer can prepare reliable bank reconciliations even when thousands of checks are outstanding and can provide current information for cash planning and forecasting .(Meigs, 1989: 385)

2.10 The Need of Internal Control

The long-run trend for corporations to evolve to organizations of gigantic size and scope, including a great variety of specialized technical operations and employees numbered in the tens of thousands, has made it impossible for corporate executives to exercise personal, firsthand supervision of operations. No longer able to rely upon personal observation as a means of appraising operating results and financial position. The corporate executive has, of necessity, come to depend upon as team of accounting and statistical reports. These reports summarize current happening and conditions throughout the enterprise: the units of Measurements employed are not only dollars but labor -hours, materials weights, customer calls, Employee terminations, and a host of their denominators.

The information carried by this stream of reports enables management to control and direct the enterprise. It keeps management informed as to whether or company policy is being carried out, whether governmental regulations are being observed, and whether financial position is sound, operations profitable, and inter departmental relations harmonious.

Business decisions of almost every kind are based at least in part on accounting data. These decisions range from such minor matters as authorizing overtime work or purchasing office supplies to such major issues as a shift from one product to another or making a choice between leasing or buying a new plant. The internal control structure provides assurance to management of the dependability of the accounting data used in making these decisions.

Decisions made by management become company policy. To be effective this policy must be communicated throughout the company and consistently followed. Internal control aids in securing compliance with company policy; management also has the direct responsibility to maintain accounting records and produce financial statements that are adequate and reliable. Internal control provides assurance that this responsibility is being met.

To the independent public accountants, internal control is of equal significance. The quality of internal controls in force, more than any other factor, determines the pattern of their examination. The independent auditors obtain an understanding of the internal control structure in order to plan the audit and to determine the nature, timing, and extent of the other auditing work necessary to permit them to express an opinion as to the fairness of the financial statements. (Meigs, 1989:149.50).

2.11 Limitation of Internal Control

Internal control can do much to protect against fraud and assure the reliability of accounting data. Still, it is important to recognize the existence of inherent limitations in any internal control structure.

Errors may be made in the performance of control procedures as a result of carelessness, misunderstanding of instructions, or other human factors. Internal control is not an effective deterrent to fraud by top management. Also, those control procedures that depend on separation of duties may be circumvented by collusion among employees. In addition, the extent of the internal controls adopted by a business is limited by cost considerations. It is not feasible from a cost standpoint to establish a control system that provides absolute protection from fraud and waste: reasonable assurance in this regard is the best that generally can be achieved. (Meigs 1989:163)

An internal control system should be designed and operated to provide reasonable assurance that an entity's objectives are being achieved. The concept of reasonable assurance recognizes that the

cost of an entity's internal control system should not exceed the benefits that are expected to be derived. The necessity of balancing the cost of controls with the related benefits requires considerable estimation and judgment on the part of management.

The effectiveness of any internal control system subject to certain inherent limitations, including management override of internal control, personnel errors or mistakes, and collusion.(Messier,2003:231)

2.12 Control Features of a Voucher System

Voucher system is one method of achieving strong internal control over cash disbursements by providing assurance that all disbursements are properly authorized and reviewed before a check is issued. In a typical voucher system, the accounting department is responsible for assembling the appropriate documentation to support every cash disbursement. After determining that the transaction is properly supported, an accounting employee prepares a voucher, which is filed in a tickler file according to the date upon which payment will be made.

A voucher, in this usage, is an authorization sheet that provides space for the initials of the employees performing various authorization functions. Authorization functions include such procedures as extending and footing the vendors' invoice determining the agreement of the transaction in the accounts. Transactions are recorded in **voucher resister** (which normally replaces a purchases journal) by an entries debiting the appropriate asset, liability, or expense accounts, and crediting vouchers payable.

Strong internal control is inherent in this system because every disbursement is authorized and \reviewed before a check is issued. Also, neither the accounting department nor the financier department is in a position to disburse cash without a review of the transaction by the other department. (Melgs, 1980:381 -385)

2.13 Internal Control for Cash Receipts Transactions

The bank reconciliation is an important part of the system of internal control over cash. Other controls of cash receipts include the separation of responsibility for recording cash transactions from the handling of cash the use of a cash short and over account for differences between recorded receipts and actual receipts, and the of cash change funds.

There are seven detailed internal control over cash objectives that internal control over cash receipts transaction must meet to prevent errors in journal and ledgers, as well as to prevent international misstatement (frauds).

The internal control over cash receipts must be sufficient to provide reasonable assurance that:-

1. Recorded transactions are valid. (validity)
2. Transactions are properly authorized. (authority)
3. Existing transactions are recorded. (completeness)
4. Transactions are properly valued. (valuation)
5. Transactions are properly classified. (timeliness)
6. Transaction is recorded at proper time. (timeliness)
7. Transaction are properly included in subsidiary ledger and correctly summarized. (summarizations)

2.14 Internal Control for Cash Disbursements

One of the best systems for establishing control of cash payments is the use. Because of the importance of taking advantage of all purchases discounts, a business may use a separate account, called discounts lost, to account for any discounts not taken during the discount period. When this method is used with the voucher system, all vouchers are prepared and recorded at the net amount, assuming that the discount will be taken.

Internal control for cash disbursement also must be sufficient to provide:-

Validity:- Segregation of duties made to check possible misstatement such as cash disbursement recorded may not be made.

Completeness:- All transaction of the given period which is made must be recorded in records. However there, might be cash disbursement made or occurred but not recorded or included.

Time lines:-All disbursement transaction must be recorded in proper time.

Authorization:- There must be proper authorization of disbursement transactions by concerned personnel.

Valuation:- The balance of cash disbursement must be properly determined. There might be incorrect amount of cash disbursed and recorded in journal. There fore there must be cash disbursements changed to wrong account.

Posting and Summarization:- All cash disbursement transaction must be posted and summarized in the proper account.

2.15 Five Important Items of Internal Controls for Cash Disbursement

Here are five items to consider when evaluation your internal controls over cash disbursements:-

1. **Segregate Duties:-** The foundation of a good internal control system is segregation of duties. The duties of authorization (signing a check or releasing a wire transfer), custody (having access to the blank check stock or the ability to establish a wire transfer), and recordkeeping should be separated so that one individual cannot complete a transaction from start to finish. The concept behind segregation of duties is that in order to misappropriate cash, individuals would have to collude, rather than one individual acting alone. For many businesses, proper segregation of duties can be difficult to achieve in these instances. Company owners may want to consider the bank statements delivered to them unopened. The owners should then review the bank statements and the check images for any transactions that appear unusual, and follow up on these transactions to obtain an understanding of them. This process alone has uncovered many situations like the one described above.
2. **Review Authorized Signors:-** Carefully consider who your authorized signors are (authorization of the transactions). Those individuals should not have access transaction into the accounting system (recording of the transaction). The use of a signature stamp, although efficient, may be problematic in that you must have separate controls to ensure that the stamp is not readily available for inappropriate use.
3. **Consider Requiring Dual Signatures:-** The comp[any may also want to consider the use of dual signatures. A dual signature policy includes the establishment of a dollar threshold over which checks require two signatures. The utilization of dual signatures establishes an element of segregation duties for disbursements over specified threshold in that these disbursements require more than one individual to authorize the transaction.
4. **Remember The Wire Transfers:-** The use of wire transfers has increased significantly over the years, and segregation of duties around wire transfers is paramount. The responsibilities for establishing wire transfer should be segregated from the responsibility of releasing the wire transfer. If this segregation is not possible, consideration should be

given to using a call-back procedure, in which the financial institution will call a specified individual when a wire transfer is initiated. Most important, the call back cannot go to any individual who is able to initiate a wire transfer.

5. **Reconcile Bank Accounts in a Timely Manner:-** The bank reconciliation should be completed in a timely manner by someone who is independent of the cash disbursement process. The bank reconciliation should also include a review of the bank statement and the check images that are returned with the bank statement for unusual transactions. Any unusual items should be investigated and evaluated when necessary.

It is never too late to review your internal controls. While processes often vary among companies, implementing the items in this checklist should significantly reduce the likelihood of your business becoming the subject of another one of those stories. (Kreischer Miller)

2.16 Consequences of Weak Internal Control Over Cash

Weak internal control procedures would create opportunity for fraud or defalcation of cash. The most common defalcation techniques of cash are:-

Withholding of Cash Receipts:- Proceeds from cash sales are withheld at point of sales recording and receiving of cash.

Lapping:- Refers to cash collection on account from credit customer may be delayed.

Fructing off bad debts:- Accounts receivable could be written off as bad debts when actually customer remittances is pocketed.

Fictions of Accounts Receivable:- Good could be taken for private use or stolen by charging fictions customers and writing off as bad debt later on.

Window Dressing:- Cash shortage or cash position could be improved by holding the cash book open/unclosed beyond the closing date to include subsequent cash receipts.

Check –Kiting:- refers transfer of check from one bank to another when the business has two bank accounts. Such technique is practiced by cashier to cover up cash shortage which an auditor might uncover.

To counter these factors, regular review of internal control system is needed to ensure that procedures are followed. These reviews are preferably done by internal auditors not directly involved in the activities. Their impartial prospective encourages an evaluation of the efficiency as well as the effectiveness of the internal control system. (Larson. 2002:354-65)

2.17 Bank Statement

A bank statement is a statement issued (usually monthly) by a bank describing the activities in a depositor's checking account during the period. A Bank statement that includes the following data:-

1. Deposits made to the checking account during the period
2. Checks paid out of the depositor's checking account by the bank during the period
3. Other deductions from the checking account for items such as service charges, NSF (non sufficient funds) checks, safe-deposit Box rent, and check printing fees.
4. Other additions to the checking account for items such as proceeds of a not collected by the bank for the depositor and interest earned on the account.

In addition to the data shown in the bank statement in above, bank statements also can show non routine deposits made to the depositor's checking account. Such deposits are not made directly by the depositor but by a third party. The bank may have received a wire transfer of funds for the depositor.

A wire transfer of funds is an inter bank transfer of funds by telephone. Companies that operate in many widely scattered locations and therefore have checking accounts with several different local banks often use an inter bank transfer of funds. These companies may set up special procedures to avoid accumulating too much idle cash in local bank accounts. One such procedure involves the use of special instruction bank accounts.

2.18 Bank Reconciliation

Bank reconciliation often called a bank reconciliation statement or schedule. It's a schedule the company (depositor) prepares to reconcile, or explain, the difference between the cash balance shown on the bank statement and the cash balance on the company's books. The bank reconciliations prepared to determine the company's actual cash balance.

The bank reconciliation is divided in to two main sections. One section begins with the balance shown on the bank statement. The second section begins with the company's balance shown on

the company's books. Adjustments are made to both the bank and book balance after these adjustments, both adjusted balances should be the same (Hermans 1992:388)

The control objectives of preparing bank reconciliation are to verify the cash book against the banks records. There by ensuring that

- a. No payments have been passed through the bank account which are not recorded in the cash book;
- b. No undue delay has occurred in paying receipt into the bank
- c. No contra items such as dishonored cheques. Which may have been paid into the bank to conceal a misappropriation, appear in the bank statement without being recorded in the cash book (Coopers, 1981:148)

The literatures reviewed so far emphasized the importance of strong internal control procedures over cash. Therefore, the next part of the paper assesses the existence of theses control procedures in National Alcohol and Liquor Factory.

According to Susan,et,al, (2005:270) the most common cause of different between the ending balance and the ending book balance of cash are as follows of outstanding cheque issued and recorded by the company but not yet presented to the bank for payment.

Deposit in transit:- Cash receipt recorded by the depositor that reached the bank too late to be included in the bank statement for the current month.

Servic charge:- Bank after charge fee handling small accounts the amount of this charge usually depend on both the average balance of and the account and the number of cheque paid during the month.

CHAPTER THREE

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

INTRODUCTION

In this chapter as it is stated at the end of chapter one, the collected data are presented in table form, analyzed by using descriptive analysis. Based on this method the characteristics of the collected facts are described in the form of frequency and percentage distribution; and the results of analyses are also interpreted and findings are identified for each item of analyses.

The student research team has collected such analyzed data from both primary and secondary data sources. For primary data, the team prepared questionnaire which consists many close ended and some open ended questions. The study is a population study because; the target population consists only the factory's finance staff members, internal auditor and the general manager, totally 7 in numbers. Even if 7copies of the questionnaire were distributed; only 6 copies were returned with responses so that the analyses are based on only the responses of such 6 respondents. In addition to this, the student research team members have observed the actual practice of the factory as of primary information. For the secondary data case the team has compiled the necessary data from the factory's financial audit report, procedural manuals, guidelines and regulations of financial activity; and analyzed together with related primary data. The analysis part is classified in to two main parts: as of analysis of characteristics the study participants and analysis of the findings of the study. This discussion is presented hereunder as follows:

3.1. ANALYSES OF CHARACTERISTICS OF THE STUDY PARTICIPANTS

Table: 3-1 description of the respondents' demography

| No | Item | Type of responses | No of Respondents | Percentage |
|----|--|---------------------|-------------------|------------|
| 1. | Respondents' sex distribution | A. Male | 4 | 66.67% |
| | | B. Female | 2 | 33.33% |
| | | Total | 6 | 100% |
| 2. | Respondents' Education level | A. Below grade 12 | 0 | 0% |
| | | B. 12 complete | 0 | 0% |
| | | C. Diploma | 0 | 0% |
| | | D. 1st Degree | 6 | 100% |
| | | E. Above | 0 | 0% |
| | | Total | 6 | 100% |
| 3. | Respondents' Service years with in the factory | A. 1 year and below | 0 | 0% |
| | | B. 2-6 years | 6 | 100% |
| | | C. Above 6 years | 0 | 0% |
| | | Total | 6 | 100% |

As per table 3.1, for the first item from the total 6 respondents 4(66.67%) are males and the rest female it implies even if it does not have negative effect to the quality of data, majority of them collected from males. The second item of table 3.1 (the respondents' educational back ground) is described as all 6 (100%) of respondents have first degree in their profession; no respondents who have under and above first degree level of education. It implies that the responses of these respondents have a highest possibility of being reasonable and reliable.

For the third item of the above table, about service year of respondents in the firm, all 6 (100%) of respondents have only 2-6 service years experience with in the firm. From the result of this analysis we can believe that even if such respondents do not have that much long period experience with in the firm, it is satisfactory for them to understand the cash controlling system of the firm because they are doing with in that system. It indicates they can provide reliable information about the factory's internal control practice over cash.

3.2. ANALYSIS OF THE FINDINGS OF THE STUDY

This part presents and analyzes the data which are related with the main research problem. This part is also classified in to three categories based on the order of research questions.

3.2.1. Assessment of the factory's internal control system over cash payment

I- Internal control over cash payment from main cash account

Table 3.2.1.1. Internal control practice over cash payment from main cash account

| No | Item | Type of responses | No of respondents | % |
|----|---|-----------------------------------|-------------------|------|
| 1. | From where your firm can get its raw materials? | A. By Making/producing by its own | 0 | 0% |
| | | B. Through purchasing | 6 | 100% |
| | | Total | 6 | 100% |
| 2. | If your answer for question No 1 is through purchasing, from where it purchases | A. From local market | 6 | 100% |
| | | B. From abroad | 6 | 100% |
| | | Total | 6 | 100% |
| 3. | How your firm is purchasing its raw materials | A. On account | 6 | 100% |
| | | B. On cash | 6 | 100% |
| | | Total | 6 | 100% |
| 4. | Does your firm have proper authorization, approval and record procedures for cash payments? | A. Yes | 2 | 33% |
| | | B. No | 4 | 67% |
| | | Total | 6 | 100% |
| 5. | In what mode does your firm make payments for purchases and other expenses | A. Cash | 6 | 100% |
| | | B. Cheque | 6 | 100% |
| | | C. Transfer | 6 | 100% |
| | | Total | 6 | 100% |
| 6. | Do you think that your firm is making payments as per its payment procedures? | A. Yes | 1 | 17% |
| | | B. No | 5 | 83% |
| | | Total | 6 | 100% |

As it is indicated in table **3.2.1.1**, 100% of the respondents indicated that they get all raw materials through purchasing. Thus there might be some problems when the transaction occurs. It indicates that the firm has huge and complex payment transactions.

For the second item of **Table 3.2.1.1**, all 100% of the respondents replied that their purchase transaction is both from local market and abroad. This indicates that there are some raw materials that can't be found in local markets.

For the third item of **Table 3.2.1.1**, all 100% of the respondents said that their firm purchases raw materials on account and on cash base. This would be good to have both options. It helps the Factory to use one in the absence of the other one.

For the fourth item of **Table 3.2.1.1**, only 33% of the respondents indicated "Yes" meaning that their firm has proper authorization, approval and record procedures for cash payments. The remaining 67% of them replied "No" to this question. This implies that there might be embezzlement and theft in the Factory.

For the fifth item of **Table 3.2.1.1**, 100% of the respondent said that payments are made through cash, cheque and transfer. As indicated in question "4" since authorization approval and record procedures are at risk, the payment instruments would also be affected.

For the sixth item of **Table 3.2.1.1**, 17% of the respondents said "Yes". The remaining 83% of them said "No" to this question. This implies that there is a serious problem in making payments as per payment procedures.

II. Internal control over cash payment from petty cash fund

Table 3.2.1.2. Internal control practice over cash payment from petty cash fund

| No | Item | Type of responses | No of respondents | % |
|-----------|---|-------------------|-------------------|------|
| 1. | Does the organization use a petty cash fund | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| | | | | |

| | | | | |
|----|---|--------------|---|------|
| 2. | Is there a maximum amount that may be drawn from the petty cash fund? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 3. | Are receipts/vouchers maintained for each expense? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 4. | Is the custodian of the petty cash fund the only one who has authorization to sign receipts/vouchers and authorize disbursements? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 5. | Does an independent and responsible employee reconcile the total vouchers with the remaining cash before replenishing the fund? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |

According to **Table 3.2.1.2.**, all (100%) respondents indicated that the factory uses a petty cash fund. Having a petty cash fund aids to save time and effort for bank withdrawal and day today recording of miscellaneous expense transactions.

For the second item of **Table 3.2.1.2.** Also all(100%) of the respondents said “Yes” it implies the factory has a limit for its petty cash fund up to 1,000 birr. In this case also its practice is in line with the known accounting guide lines.

For the third item of **Table 3.2.1.2.**, All (100%) of the respondents said that receipts/vouchers are maintained for each expense? It implies the factory has implemented the petty cash fund principles properly.

For the fourth item of **Table 3.2.1.2.**, all (100%) of respondents said “Yes”. This implies that having one authorized person reduces the risk of embezzlement. It also makes the controlling system easier. It also indicates the existence of responsible custodian for petty cash fund for controlling access for unauthorized personnel.

For the fifth item of **Table 3.2.1.2.**, all (100%) All 100% of the respondents said “Yes” when an independent and responsible employee reconcile the total vouchers with the remaining cash before replenishing the fund, cash would not be misused of embezzled. In this respect the factory is considered as established strong internal control system over petty cash.

3.2.2. Assessment of the factory's internal control system over cash receipt

Table 3.2.2.1. Internal control system over cash receipts

| No | Item | Type of responses | No of respondents | % |
|----|---|-------------------|-------------------|--------|
| 1. | Are receipts recorded by cash registers or other mechanical devices? | A. Yes | 4 | 66.6% |
| | | B. No | 2 | 33.33% |
| | | Total | 6 | 100% |
| 2. | If cash registers are used; are the machine totals independently verified by others outside of the area? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 3. | If cash registers are not used; is an independent listing of cash receipts prepared before the receipts are submitted to the cashier or bookkeeper? | A. Yes | 5 | 83.33% |
| | | B. No | 1 | 16.67% |
| | | Total | 6 | 100% |
| 4. | If yes, does a third party verify this listing against the deposit slips before receipts are recorded? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 5. | Are cash receipts deposited intact each day | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 6. | Does the factory use sales invoice and cash receipt books? | A. Yes | 6 | 100% |
| | | B. No | 0 | 100% |
| | | Total | 6 | 100% |
| 7. | If so, are they pre-numbered? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 8. | Does a non-cashier-type person independently check the numerical sequence and daily totals? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |

| | | | | |
|-----|--|--------------|---|------|
| 9. | Are all cash sales invoices accounted for daily and matched with the cash collections? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 10. | Are authenticated duplicates of the deposit slips retained and reconciled to the corresponding amounts in the cash receipts records? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 11. | Does someone prepare a daily report of cash balances? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 12. | Does the organization use mail as a cash collection mechanism? | A. Yes | 0 | 0% |
| | | B. No | 6 | 100% |
| | | Total | 6 | 100% |
| 13. | Does the employee who opens the mail maintain a listing of money, checks, and so on? | A. Yes | 0 | 0% |
| | | B. No | 0 | 0% |
| | | Total | 0 | 0% |
| 14. | If your answer is yes for the above question; does someone other than the cashier or bookkeeper open the mail? | A. Yes | 0 | 0% |
| | | B. No | 0 | 0% |
| | | Total | 0 | 0% |
| 15. | Is the list of mail receipts compared with the cash receipts book periodically? | A. Yes | 0 | 0% |
| | | B. No | 0 | 0% |
| | | Total | 0 | 0% |
| 16. | Are the unused cash sales invoice books properly safeguarded? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 17. | If none of the above is used, is some equivalent system used? Explain your practice. | A. Yes | 3 | 50% |
| | | B. No | 3 | 50% |
| | | Total | 6 | 100% |

| | | | | |
|------------|--|--------------|---|--------|
| 18. | Do adequate controls exist preventing misappropriations of cash by the cashier, such as fictitious discounts, allowances, and so on? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 19. | Do the recipients of miscellaneous receipts of cash such as those from the sale of equipment report them to the accounting department and the cashier? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 20. | Does the accounting department independently compare those reports with the related cash and bookkeeping entries? | A. Yes | 5 | 83.33% |
| | | B. No | 1 | 16.67% |
| | | Total | 6 | 100% |

As it is indicated in *Table 3.2.2.1.* 100% of the respondents replied for the first item that cash receipts are recorded by cash registers. All (100%) of such respondents indicated that the machines are independently verified by others outside of the area. This result indicates the firm's good practice in this regard.

For the third item of *Table 3.2.2.1.*, 83.33% of the respondents said yes to this question. That is an independent listing of cash receipts are made before the receipts are submitted to the cashier or bookkeeper. Listing cash receipts helps to know how many pads or volumes the cashier has received or used. Around 16.67% of the respondents replied "No". This response has some implications about the inconsistent usage of the mechanism.

For the fourth item of *Table 3.2.2.1.*, All (100%) of respondents said "Yes" for the third party verification of listings of receipts and deposit slip. This also indicates the existence of good internal control practice.

For the fifth item of *Table 3.2.2.1.*, All 100% of the respondents indicated that cash receipts are deposited intact each day. This helps the company know the number of sales on that particular day. It implies a good cash depositing practice of the factory.

For the sixth and seventh items of *Table 3.2.2.1.*, all respondents replied that the factory uses pre numbered sales invoice and cash receipt books. This is also a good internal control mechanism in order to reconcile cash sales invoices with cash receipts. Pre-numbering receipts helps to identify left out or skipped numbers. This helps to control the defected receipts. If it is not detected earlier, the receipts will be exposed to fraud or other misuse activities.

For the eighth item of **Table 3.2.2.1.**, All 100% of the respondents indicated that a non-cashier type person independently check the numerical sequence and daily totals of the pre numbered sales invoice and cash receipt books. This would be important to cross check the cashier's reports.

For the ninth item of **Table 3.2.2.1.**, 100% of the all respondents said that cash sales invoices are accounted for daily and matched with the cash collections. This assists to identify whether there is a mismatch between the two or not.

For the tenth item of **Table 3.2.2.1.**, All 100% of the respondents answered "Yes" to this question Reconciliation between the deposit slips and cash receipt records.. Reconciliation helps to check whether there is mismatch or not.

For the eleventh item of **Table 3.2.2.1.**, All 100% of the respondents said "Yes" to the question of cash balance report preparation by other independent person. This again another tool of controlling cash balances every day. It also helps the management for decision making.

For the twelfth item of **Table 3.2.2.1.**, All 100% of the respondents replied no for the question about postal collection practice of the factory, it indicates the firm doesn't use postal cash collection system.

For the thirteenth item of **Table 3.2.2.1.**, if your answer is yes for the above question; does someone other than the cashier or bookkeeper open the mail?

- The respondents didn't say any thing to this question.

For the fourteenth item of **Table 3.2.2.1.**, does the employee who opens the mail maintain a listing of money, checks, and so on?

- The respondent didn't say any thing to this question.

For the fifteenth item of **Table 3.2.2.1.**, is the list of mail receipts compared with the cash receipts book periodically?

- The respondent replied nothing to this question.

For the sixteenth item of *Table 3.2.2.1.*, all of the respondents replied “Yes” to the question of proper safe guarding practice of the factory for cash sales invoice. If they were not safeguarded, they would be exposed to embezzlement and theft.

For the seventeenth item of *Table 3.2.2.1.*, 50% of the respondents said “Yes” and the rest of them said “No” to the above question. This indicates that the 50% of the respondents were confused. Because in question 16 all the respondents said “Yes”. It can be implied that they didn’t understand the question well.

For the eighteenth item of *Table 3.2.2.1.*, all respondents answered “Yes”. For the question about the existence of proper and adequate internal control that can prevent misappropriation; However through our observation we have seen some misappropriations of cash by the cashier. All cash collections don’t deposit in a bank on daily basis.

For the nineteenth item of *Table 3.2.2.1.*, all 100% of the respondents replied “Yes” to the question of reporting miscellaneous receipts to the accounting department. It implies the record keeping for all cash receipts in the accounting department.

For the twentieth item of *Table 3.2.2.1.*, around 83.33% of the respondents replied “Yes” whereas around 116.67 % of the respondents said “No”. This implies that the accounting department independently compares those reports with the related cash and bookkeeping entries. But the no responses also indicate the existence of some inconsistency of doing such comparisons.

3.2.3. Assessment of the strength and convenience of the factory’s general internal control system over cash

Table 3.2.3.1. general internal control system over cash

| No | Items | Type of responses | No of respondents | % |
|-----------|--|--------------------------|--------------------------|----------|
| 1. | Does the factory have an organizational chart? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |

| | | | | |
|-----|--|--------------|---|--------|
| 2. | Does the factory have an organizational chart? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 3. | Does the factory have accounting and internal control manuals? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 4. | If yes, do they set forth accounting procedures? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 5. | Does the organization use a ledger system of accounting? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 6. | Is the accounting system maintained by a trained bookkeeper and/or accountant? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 7. | Does the factory use a bank account as a controlling mechanism? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 8. | Does the factory have more than one account? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 9. | Are deposits deposited by someone other than the cashier? | A. Yes | 2 | 66.67% |
| | | B. No | 4 | 33.33% |
| | | Total | 6 | 100% |
| 10. | Does a responsible employee other than the cashier investigate any debits from the deposit location? | A. Yes | 4 | 66.67% |
| | | B. No | 2 | 33.33% |
| | | Total | 6 | 100% |

| | | | | |
|-----|---|-----------------|---|--------|
| 11. | Is there a withdrawal co-signature authority process? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 12. | Does the organization have an internal auditor or equivalent person? | A. Yes | 2 | 33.33% |
| | | B. No | 4 | 66.67% |
| | | Total | 6 | 100% |
| 13. | If there is an internal auditor, is he/she independent from the internal control processes? | A. Yes | 3 | 50% |
| | | B. No | 3 | 50% |
| | | Total | 6 | 100% |
| 14. | Are periodic internal audit reports provided to the management of the factory? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 15. | What do you think about the role of internal audit reports for strengthening the internal control efficiency? | A. Yes | 2 | 33% |
| | | B. No | 0 | 0% |
| | | C. Comment | 3 | 50% |
| | | D. I don't know | 1 | 17% |
| | | Total | 6 | 100% |
| 16. | Does the head office retain adequate control over branch facilities? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 17. | Is the general accounting and bookkeeping department completely separate from the cash receipts and cash disbursement function? | A. Yes | 3 | 50% |
| | | B. No | 1 | 17% |
| | | C. Comment | 2 | 33% |
| | | Total | 6 | 100% |
| 18. | Is the general accounting and bookkeeping department separate from the sales, purchasing, and operational departments? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 19. | Are key and material bookkeeping entries approved by senior management personnel? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |

| | | | | |
|-----|---|--------------|---|--------|
| 20. | Are regular job rotations are arranged those who maintain cash, bookkeeping, asset, and/or record-keeping functions? | A. Yes | 3 | 50% |
| | | B. No | 3 | 50% |
| | | Total | 6 | 100% |
| 21. | Are regular vacations given for those who control the operational and financial activities? | A. Yes | 4 | 66.67% |
| | | B. No | 2 | 33.33% |
| | | Total | 6 | 100% |
| 22. | Are the cashier's duties segregated from the recording of cash receipts or accounts receivable? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 23. | Do procedures prohibit the cashier from gaining access to the accounts receivable ledgers or other records? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 24. | Is there more than one fund that is handled by a single cashier? | A. Yes | 2 | 33.33 |
| | | B. No | 4 | 66.6 |
| | | Total | 6 | 100% |
| 25. | If yes, please describe them | No response | | |
| 26. | Does the cashier assume full responsibility for the receipts from the time they are received until the time they are handed over for deposit? | A. Yes | 6 | 100% |
| | | B. No | 0 | 0% |
| | | Total | 6 | 100% |
| 27. | Do procedures restrict the accounts receivable bookkeeper from preparing the bank deposit? | A. Yes | 3 | 50% |
| | | B. No | 0 | 0% |
| | | C. Comment | 3 | 50% |
| | | Total | 6 | 100% |
| 28. | Do procedures restrict the accounts receivable bookkeeper from obtaining access to the cash receipts book? | A. Yes | 3 | 50% |
| | | B. No | 1 | 17% |
| | | C. Comment | 2 | 33% |
| | | Total | 6 | 100% |
| 29. | Do procedures restrict the accounts receivable bookkeeper from having access to collections from customers? | A. Yes | 4 | 67% |
| | | B. No | 2 | 33% |
| | | Total | 6 | 100% |

According to the respondent, the first item of **Table 3.2.3.1** is answered as the organization under study has an organizational; that means 100% of respondents argued this one. This is important to know the hierarchy of responsibility and to identify the main decision makers within the organization.

For the second item of **Table 3.2.3.1**, All 100% of the respondents confirmed that the organization has a chart of accounts. This helps the organization for keeping a proper record for its financial events.

For the third item of **Table 3.2.3.1**, according to the respondents the organization has accounting and internal control manuals. 100% of the respondents said that the firm has such manuals. This would be helpful to supervise and control the organization using the already set control mechanisms.

For the fourth item of **Table 3.2.3.1**, 100% of the respondents answered that they do have accounting procedures. Those procedures are significant for many purposes like accountability and for controlling each and every activity.

For the fifth item of **Table 3.2.3.1**, All 100% of the respondents said that the organization has a ledger system of accounting. This would help the organization not to underestimate and overestimate transaction. Besides, it helps as a controlling mechanism.

For the sixth item of **Table 3.2.3.1**, all the respondents answered that the factory has a trained bookkeeper and/or accountant. A trained accountant can make the accounting system to flow smoothly.

For the seventh item of **Table 3.2.3.1**, all respondents replied that the factory uses a bank account as controlling mechanisms. This would help the company to restrict the accessibility of cash to prevent the cash from the misuse.

For the eighth item of **Table 3.2.3.1**, 100% of the respondents replied that the factory has more than one bank account. This helps the company for controlling cash shortage, for loan purpose and for overdraft purpose.

For the ninth item of **Table 3.2.3.1**, 66.67% of the respondents replied that deposits are not deposited by someone other than the cashier. Whereas 33.33% of the respondents answered that there is an individual that deposits other than the cashier. This indicates that cash is exposed to embezzlement to some extent. It would be helpful if only the cashier deposits because it lays down accountability on the cashier, it also aids for segregation of duties.

For the tenth item of **Table 3.2.3.1**, 33.33% of the respondents replied that there is no other person than the cashier that investigates any debits from the deposit location. But the majority of the respondents that is 66.67% of them said that there is a responsible employee other than the cashier that investigates any debits from the deposit location. But this kind of activity leads or exposes the cash for embezzlement.

For the eleventh item of **Table 3.2.3.1**, All that is 100% of the respondents answered that there is withdrawal co-signature authority process. This helps to avoid a single person authority which in turn leads to corruption or theft free service.

For the twelfth item of **Table 3.2.3.1**, 100% of the respondents agreed or answered that the organization has an internal auditor or equivalent person. This is important for many purposes. That is for supervising the factory's finance management and it makes it ready for external auditors.

For the thirteenth item of **Table 3.2.3.1**, 50% of the respondents commented that the internal audit report has great role in resolving problems with corrective measures. And they said that the auditor is not independent from the internal control processes.

For the fourteenth item of **Table 3.2.3.1** 100% of the respondents said that periodic internal audit report is provided to the management of the factory. They also indicated that adequate control is made by following up the day to day business of the firm.

For the fifteenth item of **Table 3.2.3.1**, 33% of the respondents replied "Yes". This implies that they didn't understand the question. Whereas 50% of the respondents commented that they believe in having the role of internal audit reports for strengthening the internal control efficiency. The remaining 17% that is one respondent replied "I don't know"

For the sixteenth item of **Table 3.2.3.1** all the respondents replied that the head office provides adequate control over branch offices by following up the day to day financial activities of the business.

For the seventeenth item of **Table 3.2.3.1** half of the respondents indicated that the general accounting and bookkeeping department are completely separated from the cash receipts and cash disbursement function. And 17% of the respondent that is one respondent said "No". The rest of the respondents i.e. 33% of them commented that there is no as such a bookkeeping department but a general department.

For the eighteenth item of **Table 3.2.3.1** All the respondents indicated that the general accounting and bookkeeping departments are separate from the sales, purchasing, and operational departments. Thus this would be important for segregation of duties and as controlling mechanism.

For the nineteenth item of **Table 3.2.3.1** 100% of the respondents answered that the senior management persons approving it; however, if there is recognition by the management, the management may ratify or reject the transaction before it causes a problem.

For the twentieth item of **Table 3.2.3.1** 50% of them replied that regular job rotations are arranged for those who maintain cash, bookkeeping, asset, and or record-keeping functions while the remaining respondents replied as there is no regular job rotation arrangement. This can be viewed in two dimensions. Firstly, the respondents (50%) of them are confused whether there is job rotation or not. Having job rotation gives the employee a chance to the whole accounting system. Besides, whenever a particular employee is absent, the other employees can easily substitute and handle the job well.

For the 21st item of **Table 3.2.3.1** Around 66.67% of the respondents replied that regular vacations are given for those who control the operational and financial activities, where as 33.33% of them said that they don't get access to regular vacations. From this it can be implied that regular vacations are given although the word "regular" is considered as a relative term. Vacations are important for the productivity of the company and for making harmony among employees.

For the 22nd item of **Table 3.2.3.1** 100% of the respondents indicated that the cashier's duties are segregated from the recording of cash receipts or accounts receivable. This is very important for controlling purpose. Thus the company's control system this aspect can be considered as good.

For the 23rd item of **Table 3.2.3.1** All the respondents replied that there are procedures that prohibit the cashier from gaining access to the accounts receivable ledgers or other records. This is also another controlling mechanism of the cashier not to have access to those documents. If the cashier has access to those documents, there might be some access to delete or add unnecessary information.

For the 24th item of **Table 3.2.3.1**, 66.67% of the respondents said that there is no more than one fund that is handled by a single cashier. The rest that 33.33% of the respondents answered that there is more than one fund that is handled by a single cashier.

For the 25th item of **Table 3.2.3.1**, all the respondents left this question. Therefore this is may be lack of information or they don't want to disclose information.

For the 26th item of **Table 3.2.3.1**, 100% of the respondents replied that the cashier assume full responsibility for the receipts from the time they are received until the time they are handed over for deposit. This is good to put a responsibility on a particular.

For the 27th item of **Table 3.2.3.1**, 50% of the respondents answered "Yes" implying that procedures restrict the accounts receivable bookkeeper from preparing the bank deposit. The rest of them that is 50% of them commented that since there is no credit sales, they don't have account receivable bookkeeper.

For the 28th item of **Table 3.2.3.1**, 50% of the respondents replied that procedures restrict the account receivable bookkeeper from obtaining access to the cash receipt book. 17% of them said "No". The rest 33% of them commented that he/she does not get the access to prepare the bank deposit.

For the 29th item of **Table 3.2.3.1**, 67% of the respondents said "Yes" meaning that procedures restrict the accounts receivable bookkeeper from having access to collections from customers. The rest that is 33% of them indicated that there is no credit sale. Thus there is no account receivable bookkeeper. This implies that the respondents who said "Yes" didn't understand this question. However, through our observation there is no credit sale at all. Therefore, there is no need to have procedures that restrict the account receivable bookkeeper.

CHAPTER FOUR

SUMMARY, CONCLUSIONS & RECOMMENDATIONS

Summary of findings

The study that has been made throughout this paper is entirely devoted to the practices of internal control system with special emphasis on cash control in National Alcohol and Liquor Factory. The central theme (objective) of this study is to assess and analyze the strength appropriateness and convenience of the Factory's internal control (policies and procedures) over cash in order to identify strengths and weaknesses in the application of internal cash control.

Firstly, questioners were distributed to the target respondents. Then the data were collected and presented in table form, analyzed by using descriptive both & explanatory research designs. The student research team has collected such data from both primary and secondary data sources. For primary data, the team prepared questionnaire which consists of many close ended and some open ended questions. The study is a population study because, the target population consists only the Factory's Finance Staff Members Internal Auditor and General Manager. For the secondary data, that team has compiled the necessary data from the Factory's financial audit report, procedural manuals, guide lines etc.

- ❖ The team had taken a preliminary study and identified the existence of a researchable problem. That is the existence of cash related problem like cash shortage from daily cash sales and improper cash utilization. Hence the data obtained from the questioner and the researchers observation. Based on the previous section, the researchers formed the following summary, conclusion and recommendation in order to improve the applicability of control over cash.
- Among the total 6 respondents 4(67%) of the respondents were males where as 2(33%) of respondents were females. This implies that the male respondents are greater than female respondents.
- Regarding the respondents educational background, all (100%) of the respondents were first degree in their profession.

- As the result of the analysis indicates that all (100%) of respondents have only 2-6 service years experience with in the firm.
- The firm doesn't have proper authorization, approval and record procedures for cash payments. Most of the respondents indicated that their Factory doesn't have those procedures.
- The firm doesn't make payments as per its payment procedures. Almost 83% of the respondents answered that their firm doesn't make payments as its payment procedures.
- The study indicated that all the respondents 6(100%) confirmed that the organization uses a petty cash fund.
- As can be seen from the findings, most respondents agreed that receipts are recorded by cash registers.
- All of the respondents indicated that the Factory uses sales invoice and cash receipt books.
- Most of the respondents showed that the accounting department independently compare those reports with the related cash and bookkeeping entries.
- Most respondents that is 67% of them indicated that deposits are deposited by someone other than the cashier.
- Around 67% of the respondents showed that there is a responsible person other than the cashier that investigates any debits from the deposit location.
- The study indicated that, most respondents (67%) of them replied that there is no permanent internal auditor.
- The study indicates that there is more than one fund that is handled by a single cashier.
- The investigation confirmed that the organization uses a ledger system of accounting.
- 100% of the respondents indicated that receipts/vouchers are maintained for each expense.

Conclusion

In the beginning the student research team, identified the existence of cash shortage from daily cash sales and improper cash utilization in the preliminary study of the firm. This led the research team to assess the factory's internal control policies and procedures over cash in order to identify the real causes. The team has also studied to what extent the factory's internal control over cash is strong and convenient. Therefore from the major findings presented above, the following conclusions were made.

- According to the findings, the firm doesn't have proper authorization, approval and record procedures for cash payments. Thus this leads to misuse and theft of cash.
- The findings shows that the firm doesn't make payments as per its payment procedures. Therefore, this will result embezzlement and theft.
- The findings shows that deposits are deposited by someone other than the cashier. This implies that cash is exposed to embezzlement.
- The study also indicated that there is no permanent internal auditor. This will not allow the Factory to discover the problems in advance.
- One of the short coming that has been observed was there is more than one fund that is handled by a single cashier.
- Concerning petty cash fund, the firm properly uses the cash fund. This helps the firm to handle miscellaneous expenses well.
- The company uses sales invoice and cash receipt books. This is an important tool for controlling volume of sales.
- The firm is strong enough in using receipts or vouchers for maintain each expense.

Recommendations

Based on the findings, certain problems were identified in the study. Thus possible recommendations should be made for those problems so as to maintain the firm not to enter into a big choice or problem.

- Since the firm doesn't have proper authorization, approval and record procedures for cash payments, there should be someone who handles this activity.
- The firm should abide by its payment procedures. This would aid to follow a consistent system for all activities.
- Deposits should not be deposited other than the cashier, otherwise it might be exposed to embezzlement and other frauds.
- The firm should hire an internal auditor who always audits the firm. This will protect the cash and other assets.
- There should not be one fund that's handled by a single cashier.

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ANNEX

ST. MARRY UNIVERSITY COLLEGE

FACULTY OF BUSINESS

DEPARTMENT OF ACCOUNTING

QUESTIONNAIRES TO BE FILLED BY EMPLOYEES

ASSESSMENT OF INTERNAL CONTROL OVER CASH

THE CASE OF NATIONAL ALCOHOL AND LIQUOR FACTORY

Dear Respondent,

This questionnaire is designed with the aim of extracting desired information for our final senior research project entitled “Assessment of Internal Control Over Cash Management Practices the Case of National Alcohol and Liquor Factory.”

Since your prompt response is necessary for the research, please try to answer the questions frankly with due attention.

The questionnaire is prepared strictly for academic purpose and there is no need of writing your name.

Thank you

Please put for your responses.

I. General information about respondents’ background

1. What is your responsibility in your firm?

2. How long do you have serving in this firm? _____

3. What is your profession?_____

4. What is your academic level of qualification in your profession?_____

5. Do you think you are aright person for your position?_____

II. Data related with the main research problem

A. Questions related with the factory's internal control operation over cash payment

Internal control over cash payment from main cash account

| Questions | Alternative responses | | | Comments |
|--|-----------------------|----|---------------|----------|
| | Yes | No | I do not know | |
| 1. From where your firm can get its raw materials? | | | | |
| 2. If your answer for question No 1 is through purchasing, from where it purchases | | | | |
| 3. How your firm is purchasing its raw materials | | | | |
| 4. Does your firm have proper authorization, approval and record procedures for cash payments? | | | | |
| 5. In what mode does your firm make payments for purchases and other expenses | | | | |
| 6. Do you think that your firm is making payments as per its payment procedures? | | | | |

Internal control over cash payment from petty cash fund

| Questions | Alternative responses | | | Comments |
|--|-----------------------|----|---------------|----------|
| | Yes | No | I do not know | |
| 1. Does the organization use an petty cash fund | | | | |
| 2. Is there a maximum amount that may be drawn from the petty cash fund? | | | | |
| 3. Are receipts/vouchers maintained for each expense? | | | | |
| 4. Is the custodian of the petty cash fund the only one who has authorization to sign receipts/vouchers and authorize disbursements? | | | | |
| 5. Does an independent and responsible employee reconcile the total vouchers with the remaining cash before replenishing the fund? | | | | |

B. Questions related with the factory's internal control operation over cash receipt

| Questions | Alternative responses | | | Comments |
|--|-----------------------|----|---------------|----------|
| | Yes | No | I do not know | |
| 1. Are receipts recorded by cash registers or other mechanical devices? | | | | |
| 2. If cash registers are used; are the machine totals independently verified by others outside of the area? | | | | |
| 3. If cash registers are not used; is an independent listing of cash receipts prepared before the receipts are submitted to the cashier or bookkeeper? | | | | |
| 4. If yes, does a third party verify this listing against the deposit slips before receipts are recorded? | | | | |
| 5. Are cash receipts deposited intact each day? | | | | |
| 6. Does the factory use sales invoice and cash receipt books? | | | | |
| 7. If so, are they pre-numbered? | | | | |
| 8. Does a non-cashier-type person independently check the numerical sequence and daily totals? | | | | |
| 9. Are all cash sales invoices accounted for daily and matched with the cash collections? | | | | |
| 10. Are authenticated duplicates of the deposit slips retained and reconciled to the corresponding amounts in the cash receipts records? | | | | |
| 11. Does someone prepare a daily report of cash balances? | | | | |
| 12. Does the organization use mail as a cash collection mechanism? | | | | |
| 13. If your answer is yes for the above question; does someone other than the cashier or bookkeeper open the mail? | | | | |

| | | | | |
|--|--|--|--|--|
| 14. Does the employee who opens the mail maintain a listing of money, checks, and so on? | | | | |
| 15. Is the list of mail receipts compared with the cash receipts book periodically? | | | | |
| 16. Are the unused cash sales invoice books properly safeguarded? | | | | |
| 17. If none of the above is used, is some equivalent system used? Explain your practice. | | | | |
| 18. Do adequate controls exist preventing misappropriations of cash by the cashier, such as fictitious discounts, allowances, and so on? | | | | |
| 19. Do the recipients of miscellaneous receipts of cash such as those from the sale of equipment report them to the accounting department and the cashier? | | | | |
| 20. Does the accounting department independently compare those reports with the related cash and bookkeeping entries? | | | | |

C. Questions related with the factory's general structure of Internal Control over Cash

| Questions | Alternative responses | | | Comments |
|---|-----------------------|----|---------------|----------|
| | Yes | No | I do not know | |
| 1. Does the factory have an organizational chart? | | | | |
| 2. Does the factory have a chart of accounts or an organized financial accounting system? | | | | |
| 3. Does the factory have accounting and internal control manuals? | | | | |
| 4. If yes, do they set forth accounting procedures? | | | | |
| 5. Does the organization use a ledger system of accounting? | | | | |
| 6. Is the accounting system maintained by a trained bookkeeper and/or accountant? | | | | |
| 7. Does the factory use a bank account as a controlling mechanism? | | | | |
| 8. Does the factory have more than one account? | | | | |

| | | | | |
|---|--|--|--|--|
| 9. Are deposits deposited by someone other than the cashier? | | | | |
| 10. Does a responsible employee other than the cashier investigate any debits from the deposit location? | | | | |
| 11. Is there a withdrawal co-signature authority process? | | | | |
| 12. Does the organization have an internal auditor or equivalent person? | | | | |
| 13. If there is an internal auditor, is he/she independent from the internal control processes? | | | | |
| 14. Are periodic internal audit reports provided to the management of the factory? | | | | |
| 15. What do you think about the role of internal audit reports for strengthening the internal control efficiency? | | | | |
| 16. Does the head office retain adequate control over branch facilities? | | | | |
| 17. Is the general accounting and bookkeeping department completely separate from the cash receipts and cash disbursement function? | | | | |
| 18. Is the general accounting and bookkeeping department separate from the sales, purchasing, and operational departments? | | | | |
| 19. Are key and material bookkeeping entries approved by senior management personnel? | | | | |
| 20. Are regular job rotations are arranged those who maintain cash, bookkeeping, asset, and/or record-keeping functions? | | | | |
| 21. Are regular vacations given for those who control the operational and financial activities? | | | | |
| 22. Are the cashier's duties segregated from the recording of cash receipts or accounts receivable? | | | | |
| 23. Do procedures prohibit the cashier from gaining access to | | | | |

| | | | | |
|---|--|--|--|--|
| the accounts receivable ledgers or other records? | | | | |
| 24. Is there more than one fund that is handled by a single cashier? | | | | |
| 25. If yes, please describe them | | | | |
| 26. Does the cashier assume full responsibility for the receipts from the time they are received until the time they are handed over for deposit? | | | | |
| 27. Do procedures restrict the accounts receivable bookkeeper from preparing the bank deposit? | | | | |
| 28. Do procedures restrict the accounts receivable bookkeeper from obtaining access to the cash receipts book? | | | | |
| 29. Do procedures restrict the accounts receivable bookkeeper from having access to collections from customers? | | | | |