

Accounting Case Exploration

Staff Auditor for Public Accounting Firm

TEACHERS GUIDE

Overview:

This lesson plan will introduce students to the world of accounting by placing them in a real-life situation as an accountant. Divide your students into groups of 3-4 and distribute the accounting case to each group. Review the prompt with the class and have them come up with a collective recommendation after reviewing all considerations.

Team review of accounting case: 20 minutes

Group presentation: 5-10 minutes per group

Accounting Case:

You are a staff auditor for Acme Accounting, a public accounting firm. Acme Accounting has performed the accounting audit for Ag Essentials agricultural products and services company for the past five years. Ag Essentials is a fairly small company with an office receptionist, Susan, an accounts receivable clerk, Kelly, and an accounts payable clerk, Terry. The daily deposits and monthly bank reconciliations are handled by Kelly, who is one of the “most dedicated and honest employees” the manager, Bob, has ever known. In fact, Kelly has worked at Ag Essentials longer than anyone else in the office, and she hasn’t called in sick in the past two years. She is single with a son in college, and has opted to take the company’s vacation “pay out” in order to receive more money and has not taken a week-long vacation in years. Everyone at Ag Essentials loves their job because farmers are some of the best customers in the world! The farmers really enjoy Kelly, too, as they have gotten to know her over the years, and many will come in and pay their monthly statement directly with Kelly, some pay by check and some pay with cash.

During a recent audit while examining the accounts receivables, you notice that several customers’ annual account purchases have decreased from prior years. This may not be cause for concern, as often farmers will “spread their business around.” Since most of the farmers’ accounts that you examined had, in fact, increased at approximately the same percentage, you decide to speak with the manager. Bob indicates that business has been great, despite the recession. In the Ag business, farmers still need to buy seed, fertilizer and chemicals regardless of the state of the economy.

Finally, you mention three customer accounts that appear to have dropped off in purchases as compared to most of the other customers and ask Bob if he is aware of this decrease. You can tell by the expression on Bob’s face that he seems to be confused, and he explains to you that he is pretty sure there has not been any decrease in their purchases. Now Bob frowns as he mentions that these customers are among the farmers who regularly pay in cash, as opposed to check. He also admits that he doesn’t pay that close attention to customer accounts that are keeping up with their payments. His time has been spent focusing on the past due accounts.

At the end of the day when Kelly goes home, Bob discovers a second cash receipt booklet that she had apparently been using to write receipts for the full amount of cash the farmers were paying, but then using another one to write the actual receipt for the amount she would then deposit in the bank. Kelly also had two sets of accounts receivable invoices she had been keeping for these customers, the actual invoice for what they had purchased and the invoice she would use for company records that would enable her to pocket a good portion of their cash payments each month. It turns out the state of the economy was affecting Kelly in ways that Bob, nor her co-workers, nor her farmer friends ever realized.

Considerations:

- As an auditor for Acme Accounting, what “red flags” do you see throughout this scenario?
- What advice would you give Bob to help him establish effective internal controls?
- How should Bob handle the situation with Kelly?
- A discussion about trust and the human factors that go into putting trust in employees, as well as how difficult it is to build back trust in someone once that has been broken would be a good discussion to have as well.
- Explore the Fraud Triangle to examine what motives might exist.

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Solution:

Students may identify the following as “red flags”:

- Office duties are not rotated.
- The bank reconciliation is being performed by an individual who handles cash daily.
- An employee never takes off due to illness or for vacation.
- There is no required vacation leave, since the company will pay employees who don't take off.
- There could be more “red flags.”

Students may suggest the following to help Ag Essentials establish effective internal controls:

- Rotate the duties of the office staff, so that each one knows how to handle all office responsibilities.
- Have the bank reconciliation task performed by the receptionist, since she doesn't handle cash on a regular basis, nor does she write the checks.
- Require vacation leave to be taken by employees.
- Bob should pay more attention to the customer accounts, and run some random reports that would compare what is being invoiced to what the warehouse and drivers' records report.
- Establish inventory controls that would make it difficult to falsely invoice customers.
- Eliminate hand-written receipts for cash payments, and require customer payments to be entered on a computer immediately with a printed receipt. The auto numbering of the receipts would add to the control.
- Possibly have the receptionist take payments from customers, with the understanding that if customers have questions or issues with their account, the A/R specialist would be asked to come out to the reception area to assist. With all office staff understanding the function of A/R, it would be hopeful that the amount of questions about an account that only A/R could answer would be minimized.
- Other controls that students might think of could have to do the IT controls, where login/password requirements for the office accounting software would enable all activity in the system to be documented by user, which could further help identify who may be responsible for future questionable actions.

Students may suggest the following as ways Bob can handle the situation with Kelly:

- Fire her on the spot.
- Sit down with her and the auditor to discuss what was found and see what her reaction is to the accusations.
- Give her a second chance, knowing that the controls he is putting in place will considerably reduce her ability to do additional damage.
- They need to factor in issues such as trust and the human factors that go into putting trust in employees, as well as how difficult it is to build back trust in someone once that has been broken would be a good discussion to have as well.