VII. ACCOUNTS PAYABLE AND PURCHASES

Internal control objectives

- Goods or services are purchased only with proper authorization.
- Goods or services received are recorded correctly as to account, amount, and period.
- Recorded acquisitions are for goods and services received.
- Adjustments to vendor accounts are made in accordance with management's authorization.
- Only authorized goods and services are accepted and paid for.
- Access to purchasing, receiving, and accounts payable records is adequately controlled to prevent or detect duplicate or improper payments.

Potential errors and fraud

- Unauthorized purchases are incurred.
- Purchases are recorded but goods or services are not received.
- Liability is incurred but not recorded.
- Purchase amount is recorded incorrectly.
- Purchase is charged to wrong account or is recorded in wrong period.
- Purchases at other than favorable terms are made to facilitate side deals for the personal benefit of employees.
- Purchases are misclassified to conceal lack of authorization.
- Improper deferrals of income are recorded in order to shift income to future periods.
- Purchase discounts are taken but not recorded and amounts of discounts are misappropriated.
- Employees conceal unauthorized purchases for their own benefit.

Understanding of accounting system

1. Describe how and by whom transactions are initiated and authorized.

2. Describe the procedures, both automated and manual, by which transactions are recorded, processed, and reported from their occurrence to their inclusion in the financial statements.

3. Describe the source documents that support the transactions.

4. Describe the computer media that is used in the processing of accounting information.

5. Describe the documents and reports generated by the accounting system.

**Further understanding of control activities**

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<th>YES</th>
<th>NO</th>
<th>N/A</th>
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1. Does the client have a purchasing department? If yes, is it independent
of:

a. The accounting department?

b. The receiving department?

c. The shipping department?

2. Are purchases made only after the respective department heads sign purchase requisitions?

3. Are purchases made by means of purchase orders sent to vendors for:

a. All purchases?

b. Only purchases over a predetermined dollar limit?

4. Do purchase orders specify:

a. Description of items?

b. Quantity?

c. Price?

d. Terms?

e. Delivery requirements and dates?

5. Is a list of unfilled purchase orders maintained and reviewed periodically?

6. Are purchase order forms prenumbered and is the sequence accounted for periodically?

7. Does the client maintain an approved vendors list?

8. Are items purchased only after competitive bids are obtained? If yes, are competitive bids obtained for:

a. All purchases?

b. Only purchases over a predetermined dollar limit?
9. Is a log maintained of all receipts?

10. Does the receiving department prepare receiving reports for all items received? If yes, are receiving reports:
   a. Prepared for all items?
   b. Prepared only for items that have purchase orders?
   c. Prenumbered?

11. At the time the items are received, does someone independent of the purchasing department check the merchandise before acceptance as to:
   a. Description?
   b. Quantity?
   c. Condition?

12. Are copies of receiving reports:
   a. Furnished to the accounting department?
   b. Furnished to the purchasing department?
   c. Filed in the receiving department?

13. Are receipts under blanket purchase orders monitored, and are quantities exceeding authorized total returned to vendor?

14. Are procedures adequate for the proper accounting for partial deliveries of purchase orders?

15. Are purchasing and receiving functions separate from invoice processing, accounts payable, and general ledger functions?

16. Are vendors' invoices, receiving reports, and purchase orders matched before the related liability is recorded?

17. Are invoices checked as to:
   a. Prices?
b. Extensions and footings?  

YES  NO  N/A

c. Freight charges or allowances?  

YES  NO  N/A

d. Credit terms?  

YES  NO  N/A

18. Are controls adequate to ensure that all available discounts are taken?  

YES  NO  N/A

19. Are purchases recorded in a purchase register or voucher register before being processed through cash disbursements?  

YES  NO  N/A

20. Does a responsible employee assign the appropriate general ledger account distribution to which the invoices are to be posted?  

YES  NO  N/A

21. Are procedures adequate to ensure that invoices have been processed before payment and to prevent duplicate payment (e.g., a block stamp)?  

YES  NO  N/A

22. Does a responsible official approve invoices for payment?  

YES  NO  N/A

23. Are procedures adequate to ensure that merchandise purchased for direct delivery to customers is promptly billed to the customers and recorded as both a receivable and a payable?  

YES  NO  N/A

24. Are records of goods returned to vendors matched to vendor credit memos?  

YES  NO  N/A

25. Are unmatched receiving reports, purchase orders, and vendors’ invoices periodically reviewed and investigated for proper recording?  

YES  NO  N/A

26. Is the accounts payable ledger or voucher register reconciled monthly to the general ledger control accounts?  

YES  NO  N/A

27. Are statements from vendors regularly reviewed and reconciled against recorded liabilities?  

YES  NO  N/A

28. Do adjustments to accounts payable (e.g., writing off of debit balances) require the approval of a designated official?  

YES  NO  N/A

29. Are budgets used? If yes:  

a. Are budgets approved by responsible officials?  

YES  NO  N/A
b. Are actual expenditures compared with budgeted amounts and variances analyzed and explained?


30. Are entries for deferrals of income reviewed to assure that they result in proper recognition of income?


Assessment of control risk
(Maximum, Slightly Below Maximum, Moderate, or Low)

<table>
<thead>
<tr>
<th>Assessment of control risk</th>
<th>Existence or Occurrence</th>
<th>Completeness</th>
<th>Rights and Obligations</th>
<th>Valuation or Allocation</th>
<th>Presentation and Disclosure</th>
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