A FORENSIC ACCOUNTING INTEGRATED CASE

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CASE DESCRIPTION

The subject matter of this case consists of three parts. The first part involves the effects on financial statements of recording fictitious transactions and the effects on financial statements of not recording required transactions. The second part involves the analysis of financial information when there are apparent (or should be apparent) inconsistencies between the information reported in the financial statements and other provided information. The third part consists of the analysis of an internal accounting control system that contains some areas of weakness.

This case can be useful in any accounting course after basic accounting topics, including internal control, have been covered. All three parts of the case have been student tested in a Forensic Accounting course after the applicable topics were reviewed in class. The individual parts, or the entire case, can be assigned either as an in-class/group project, take home assignment, or in-class exam.

This case has improved student learning when used relatively early in a Forensic Accounting course as it provides a solid base of the rules surrounding financial accounting and internal control that students need to solve advanced forensic accounting cases. When combined with lecture this case will help get students "up to speed" with their understanding of financial accounting relationships and internal control.

CASE SYNOPSIS

This case provides a practicable example of a small business that has just begun operations and is experiencing business and accounting issues. There are multiple topics included in the case. First, is a real world example of a business recording inappropriate transactions and failing to record appropriate transactions, in order to produce financial statements that reflect a financial position and results of operations that is better than the application of Generally Accepted Accounting Principles (GAAP) would produce.

The information contained in financial statements may look perfectly acceptable, prior to closer scrutiny. There are danger signs that accountants and other users of the financial statements should be aware of. The second part of this case provides an opportunity for students to analyze financial data based on financial relationships and other information to determine whether additional information may be required to determine the accuracy of the financial statements and their component parts.

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Third, small businesses with few employees have a built in disadvantage with regard to the application of appropriate internal control. This case provides an opportunity for students to apply some basic concepts of internal control to a business that contains weaknesses that occur in real world situations.

INSTRUCTORS' NOTES

Part 1: Facts and Requirements

Facts--Financial Information at the End of the First Year of Operations

Big Al was aware that Big Al's Pumps experienced cash flow problems in the later part of 2012. During the first week of December 2012 he confided to Martha that he was worried that the lender, Valley Bank, would be unhappy with the first year financial results and might even demand immediate repayment of the loan. He asked Martha if there was anything she could do to make the financial statements "look better".

The year-end for Big Al's Pumps is December 31, 2012, a Monday. Martha said she could keep the books open through January 11, 2013 for transactions involving sales of inventory and cash collections of accounts receivable. She added that she would make the fictitious sales of inventory on credit only, no cash sales, for the sake of simplicity. Martha told Big Al she would treat the cash collected through January 11, 2013 as a deposit of cash in December 2012 and a deposit in transit on the December 31, 2012 bank statement. She would reduce Inventory at December 31, 2012 to reflect the sales for the period during 2013 that would be treated as 2012 sales. Martha assured Big Al that even though the transactions would be recorded in the wrong period the books would be in balance as of December 31, 2012 and the cash in the general checking account would agree to the December 31, 2012 bank reconciliation. She also told Big Al she could record the sales discounts taken by customers during the month of December 2012 in January 2013.

Requirement 1: Read the Introduction and Facts provided and prepare the journal entries for all the transactions described by Martha in the 'Financial Information at the End of the First Year of Operations'. Use the journal entry format provided in Figure 1. Number your journal entries because you will use each journal entry number in Requirement 2. Record the journal entry required by GAAP in the Correct column when the transaction required the journal entry at 12/31/2012; if the transaction did not require a journal entry at 12/31/2012 write 'no entry' in that column. Place the journal entry in the Actual column when Martha made a journal entry at 12/31/2012; if Martha did not record a journal entry for the transaction at 12/31/2012 write 'no entry' in that column.

Requirement 2: Based on the journal entry numbers from Requirement 1 and using the format provided in Table 1—Format for Overstated and Understated Accounts, record the

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