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Internal control for cycle billing systems in department and speciality stores

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INTERNAL CONTROL

FOR

CYCLE BILLING SYSTEMS

IN

DEPARTMENT AND SPECIALTY STORES
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PREFACE

Increased use of credit selling by department and specialty stores and the initial use of credits by some variety stores have magnified the problems of internal control of billing and other account receivable activities. Cycle billing systems have been widely adopted in an attempt to handle this larger volume expeditiously and at the lowest possible cost. This paper is intended to make available the current results of a study and investigation of cycle billing control problems. It deals with the nature of the problems involved, the relative advantages and disadvantages of the types of control systems now in use, and general rules of internal control procedures for cycle billing systems. While the material presented is primarily suitable for the larger store, it applies in many instances to the smaller store. It is assumed that the typical reader will be thoroughly familiar with retail terminology.

The general problem of internal control involves relationships among departments as well as control features within each department. This statement treats only of the control problems of account receivable departments primarily with respect to cycle billing systems. It does not deal with related problems such as the numerical control over sales-checks, the issuance of salesbooks and credit books, the processing of incoming mail, the handling of deposits representing collections on receivables, charge authorization procedures and credit policy.

Volume of account receivable media determines, at least in part, the relative need as well as the feasibility of adoption of various control techniques. Thus some stores may find it difficult to put into effect all the control features mentioned in this statement. It is important that the risk involved in
departing from the basic rules of internal control be carefully evaluated.

Changing conditions may materially affect the calculated risk. Thus when a calculated risk is taken an orderly procedure of periodic and continuing review of the decision should be established. Only in this way is it possible to assure intelligent risk-taking in stream-lining and short-cutting traditional procedures.

The practicability of use of various control systems and the extent of the calculated risks to be taken are determined, in part, by the cost of operating the alternative systems. Research on the comparative costs of various cycle billing systems is being actively carried on; however, cost data are not included in the scope of this preliminary statement because of the time which will be required to obtain reliable data incorporating all of the factors which must be considered.

Although some of the basic internal control rules set forth in this statement are general in their application, primary emphasis is given to situations where conventional bookkeeping machines are in use. Thus particular procedures required by the use of punched card or electronic equipment are not treated at this time.

We wish to acknowledge a number of useful suggestions by store control and financial executives.

Touche, Niven, Bailey & Smart

New York
August 15, 1958
EVOLUTION OF BILLING SYSTEMS

Accounts receivable from customers represent the largest single asset of department and specialty stores which offer credit facilities. Such accounts, on the average, comprise about 45% of current assets and 35% of total assets. The average gross sales transaction (cash and credit) is about $5.00. The average for credit transactions is somewhat higher. Typically, stores with credit facilities will carry thousands of individual customer's accounts with the largest stores handling in excess of a half million accounts.

Prior to World War II the prevalent billing system for customers' accounts (referred to hereinafter as end-of-month billing) involved the preparation of a statement for each customer as of the end of each calendar month. Each transaction was posted on the statement with a short description or identification of the purchase, return, or payment. All statements were mailed as of the end of the month, with the store keeping a copy of the statement in the form of a ledger page, a duplicate statement, or a microfilm. The media (saleschecks, credits and cash payment slips) were retained by the store for reference purposes. Generally control accounts were established for each ledger, which included from 500 to 1,000 accounts. Upon completion of the month's posting (done in four or five "batches" of four to six days' media each), the statements were mailed. Trial balances were taken of each ledger, and differences between trial balance details and controls were customarily reconciled to the penny. Often the statements were not mailed until the reconciliations were complete.

The high cost of doing business has prompted stores constantly to seek economies in order to maintain shrinking profit margins. One of these econ-
omies, which emerged in the early forties, involved the replacing of expensive end-of-month billing plans with cycle billing systems. Over the last ten to fifteen years the acceptance of cycle billing has spread to the extent that it is used today, in one form or another, in almost all except the smallest stores.

Cycle billing refers to the method of maintaining and billing of customers' accounts receivable. Under this plan customers receive statements once during each month, showing purchases, credits, payments and balances, covering a 30-day period. In the typical situation, customers' account files are divided into cycles, on an alphabetical basis, and each of these cycles is billed once a month, as of a specified cut-off date. The cycle billing dates are staggered throughout the month to spread the billing load as evenly as possible over all the working days of the period. These cycle billings include all transactions affecting the accounts within the cycle from the cut-off date in the prior month to the current billing date.

At the time of billing a cycle, approximately thirty days' volume of the store's transactions with customers within that cycle are represented by loose pieces of paper in the customers' account files. Since only one cycle is billed on any one day, the customers' account files on any given day contain pieces of paper supporting an average of one half a month's volume of the store's credit transactions. The existence of this loose unproven media at the end of monthly accounting periods presents a major problem in a cycle billing operation and represents the principal challenge to any cycle billing control system. This problem is further compounded by the extent of employee access to these loose media. For example, in a typical store with adequate internal control and an annual volume of $30,000,000, there may be 75 to 100 persons who have authorized access to accounts receivable files at all times.
The details which support control accounts are usually established in an accounting system by listing all the items and comparing the result with the general ledger balance at the end of the month or other cut-off date. Typical examples of this technique are the physical inventory of merchandise, the count of cash and the trial balance of accounts payable. The trial balance of accounts receivable as developed under the superseded end-of-month billing plan provided this type of control. As explained later in this paper different cycle billing systems provide this tie-in in different ways and in varying degrees. Each of the systems involves risks and it is the responsibility of management to evaluate the risks taken. The cycle billing control system chosen should be one which, with reasonable assurance, will permit an accurate evaluation of billing results when compared with the predetermined figures each month.

CYCLE BILLING CONTROL SYSTEMS

There are three distinct types of accounts receivable cycle billing control systems in common use by department and specialty stores. They are the one-control system, the cycle control system and the two-control system. Many variations and combinations of the elements of these systems are possible, and only the basic framework will be included in the discussions which follow. A summary of the advantages and disadvantages of the three types of systems is presented in Exhibit A on pages 27 through 30. The term "end-of-month" as used in these discussions is intended to mean the end of the store's accounting period. The term "control" refers to those records maintained in the accounts receivable department. References to a general ledger account are made explicitly.
ONE-CONTROL SYSTEM

End-of-month balance of accounts receivable is established under this system by adding to the totals of cycles billed during the month a physical inventory of the unbilled transactions (media) affecting these cycle balances as of the end of the month. The total of the cycles billed plus this physical inventory should agree with the general ledger balance of accounts receivable, which is the control account under this system.

Theoretically, the operation of this system provides an accurate determination of the balance of the accounts receivable detail at the end of each month. It is the only cycle billing control system which does not defer to the following period the verification of the existence of the unbilled media. Since the unbilled media are filed by customer, as a practical matter the taking of a physical inventory of the unbilled media as of one cut-off date creates a tremendous work load in cases where the number of active customers' accounts is great. The margin of human error involved in taking the physical inventory in a large store is often great enough to negate this procedure as a reliable control device. This system, therefore, has greater appeal to smaller stores. It is seldom used in very large stores except on an occasional experimental basis.

In some instances where the one-control system is used, the physical inventories of unbilled transactions are taken only periodically – every three, six or twelve months or the cut-off date is established at other than the end of the month. Since the principal advantage of the one-control system is the valuation of all loose media and the determination of differences at the end of each month, practices such as these nullify to a great extent the effectiveness of this system.
CYCLE CONTROL SYSTEM

This system provides for the maintenance of individual control accounts for each cycle or billing segment, which are to be compared in total with the general ledger account. The number of cycle controls to be maintained is a matter of individual store preference, and in practice is found to range from a few to 120 or more. Sixteen to twenty controls are the most common.

The objective of the cycle control system is to establish controls over small segments of the accounts which will provide for immediate comparisons with the results of the billing of the segments, and allow for immediate action to be taken to locate and correct differences, if any. The mechanics of the system are as follows:

On a daily basis, the sales audit department breaks down the totals of sales, credits, cash and other transactions by cycles and transmits this information to the accounts receivable control clerk. Daily, the control clerk posts the individual figures, by type of transaction, to the individual cycle control records maintained for that purpose. In addition, the daily totals for all cycles combined, by type of transaction (sales, credits, cash, etc.), are posted to a master control record. At the end of the month, the sum of the daily figures developed by sales audit is posted to the general ledger which, at this point, should agree with the master control account, which in turn is supported by the balances in the individual cycle controls.

As of the cut-off date for a cycle, the control clerk determines from the control account for that cycle, the totals of the various types of transactions and the balance of the cycle as of that date. Theoretically these figures should be the same as those on
the billing tape for that cycle when the billing has been completed. Since the comparison with the billing tape can be made by type of transaction, differences may be localized and immediate investigation is possible, even before the statements are mailed. This procedure is repeated for each of the cycles billed during the month.

The reconciliation of billing tape totals and the cycle control accounts is usually complicated because of items charged to the cycle control but not included in the billing for one reason or another. The most common of these are "throw-outs," a term applied to any item which a biller fails to include in the billing run -- even if it is excluded by mistake. "Throw-outs" can result from a wide variety of causes such as illegible amounts, misfiled media not previously detected and items misplaced or lost until the run is completed. The media thus excluded from the billing become reconciling items between the detail and control.

As previously noted, the end-of-month total of the controls maintained by the control clerk should equal the master control which in turn should be in agreement with the general ledger. Since billings of cycles are staggered over the entire month, there remains in the end-of-month master control balance an average of approximately one-half month of transactions which are supported only by the daily entries to the control accounts. These items become part of the comparison with the billing results of that cycle in the following month. Complete control over the unbilled amounts remaining in all cycles at the end of the month will not have been accomplished until these items have been included in the billing of these cycles in the following month. On the other hand, it should be noted that under the cycle control system, the billing of each cycle can be looked upon as a physical inventory of all media in the cycle as of the cut-off date.
Variations of the procedure explained above are sometimes used. For example, one group of stores arranges for a proof of accounts receivable as of the end of a fiscal month by having sales audit during the month stamp all media which would be unbilled as of the end of the month, and by having someone independent of the accounts receivable and credit departments develop totals of these media before stuffing. At the end of the month the unbilled media totals plus the balances for cycles closing during that month are compared to the general ledger figure, independently of the cycle controls.

TWO-CONTROL SYSTEM

This type of system provides a comparison of a general ledger figure, as of the end of the month, with the sum of the billing trial balance of all cycles billed during the month plus the total of all unbilled media as of the end of the month. The term "two-control" refers to the mechanics of the system which provides for establishing control of the totals of transactions in two parts, one of which is the computed unbilled portion.

Within this category, two variations of a control system are recognized, which, for purposes of identification, may be referred to as (a) the two-control system with a pre-billing, daily split of media, and (b) the two-control system with a post list split of media. Both of these systems are methods of control for all cycles in total only. The control under the post list system requires an extra thirty days to determine differences. The mechanics of these systems are as follows:

Pre-billing and daily split of media. The basic control figures for this system are established daily by sales audit. Upon completion of the daily balancing procedures, sales audit sorts each type of media
(sales, credits, cash) into its proper billing cycle. As under all cycle billing systems these cycles are established on an alphabetical basis and, to facilitate stuffing, the media for each cycle are grouped separately. Based upon predetermined cycle cut-off dates, each day sales audit determines (1) which cycles will be billed before the end of the month and (2) which cycles will not be billed until the following month (i.e., because the current month's billing dates for these cycles have already passed.) Sales audit then develops the control figures by totaling the media for each of the groups of cycles. These totals are given to the control clerk who enters them in a record showing daily figures for "billed," "unbilled" and the total of the two (master control). The accounts receivable master control account and the general ledger should always be in agreement; normally there should be no reconciling items.

At the end of the month, the control clerk accumulates the billing trial balance totals (charges, credits, cash, etc.) for all the cycles billed during the month. To these totals are added the balances in the unbilled control account. The sum of these items should agree with the balance in the master control account and also with the general ledger. In a reconciliation of this type, the actual existence of media representing the "unbilled" total included in the reconciliation (which averages approximately one half a month's media) cannot be supported until the end of the next month. At that time the billed media originating in the subsequent month can be subtracted from the total media actually billed during the later month, to establish the amount of prior month media included. This figure should agree with the balance in the unbilled control at the end of the prior month.

As a variation of the procedures explained above, one store subdivides its accounts receivable into three sections on an alphabetical basis and
separately applies the billed and unbilled procedures to each of the three sections, as if each section represented the accounts of a different store.

Post list split of media. The outstanding characteristic of the post list system is that the control is established after billing using hindsight. No attempt is made, on a day-to-day basis within the month, to predetermine what the billing results will be. This system operates as follows: Each day after the media have been processed by sales audit they are marked in some manner which will identify their month of origin. This is usually accomplished by running the media through a tickometer, which marks the media with a monthly identification and, in most cases, a date. No further control is established over these media until after they are billed.

When the billing of a cycle has been completed, the statements and media are given to a post-lister. The post-lister runs a tape which splits the media by type (cash, credits, charges, etc.) and by month of origin (i.e., current month or prior month) based on the marking previously placed on the media. The total of the split tapes (current and prior month) should agree with the total on the biller's tape. This comparison is a check of the biller's accuracy. Any differences between the biller's totals and the post-lister's total are investigated and appropriate corrections made. The corrected totals are then entered on a control sheet showing month of origin of the media (current month and prior month). Such totals are entered by cycle and by type of media. This process is repeated for every cycle billed during the month. At the end of the month, the sum of the media billed this month which originated in the prior month and the media billed last month which originated in that month should agree with last month's total media given to the accounts receivable department.
Since the post list controls are established only on billed balances, there remains in the files at the end of each month, approximately one half of the current month's media over which no control or proof of existence has been established. The control over these media is established by a similar procedure performed in the next month. Under this system, therefore, a comparison of the control account balance with the general ledger balance for any given month can be made only after the end of the subsequent month.

In some instances where a post list split is made, the sales audit department establishes figures for cycle controls as to sales media only. Transfers between cycles are not recorded. This type of control is superimposed on the existing control system to provide a basis for quickly determining upon the completion of the billing of a cycle that no significant difference exists between the input of sales media and billings to the customer.

Variations of procedures. Two variations of procedures may be noted in the use of two-control systems. The split of media by month of origin may be done as a part of the billing operation (rather than by pre-billing split or post list) and the bookkeeping machine registers may develop separate totals for "this month" and "last month."

In a hybrid type of two-control system a store maintains an unbilled sales control account and an unbilled credit control account in addition to a control for billed accounts receivable. In addition, cycle controls are maintained for cash payments. Upon completion of the billing of a cycle, the bookkeeping machine totals for sales and credits are transferred from the unbilled control accounts to the billed accounts receivable control account. The cash totals from the machine are compared to the cycle controls for cash but no control entry is required because the
total of cash receipts was originally credited to billed accounts receivable. Thus, at the end of the month (or at any other point), the balances shown by the unbilled control accounts reflect the amounts of unbilled saleschecks and credits in the cycle files. Quarterly, this store "proves" the total of the unbilled controls by having the sales audit department split the sales and credit media into totals for "billed" and "unbilled" for an entire month to develop an aggregate unbilled figure of sales and credits for comparison with the corresponding controls.
TRANSFER PROBLEMS

A major problem under cycle billing is the handling and recording of transfers of amounts between different control accounts. As used here, the term transfer refers to the correction of an original mis-classification of media either by type of account (regular, budget, installment) or by cycle (missorts).

TRANSFERS BETWEEN TYPES OF ACCOUNTS

The problem of transfers between types of accounts exists only if separate control and general ledger accounts are maintained. If more than one general ledger and control account are to be accurately maintained for the various types of accounts, transfers between the separately controlled types of accounts must be made under all systems.

The volume of such transfers obviously is determined by the number of misclassifications in the initial handling of media. These misclassifications are usually due to incomplete or incorrect information on the media. Although misclassifications are numerous, the problem lies not in the physical transfer of the media but in establishing the transfer entries for the separately maintained control and general ledger accounts.

Where the various types of accounts are interfiled, the misclassification of customers' media between types of accounts can be physically corrected on the spot by the unit clerk. This physical transfer is not the entire correction, however, because an adjustment of the accounts receivable control account and the general ledger must still be made.

The form used for the adjustment may be (1) the piece of media itself or (2) a separately prepared
transfer form. If media are used they must be reprocessed and the transfer recorded before they can be stuffed into the proper accounts. If transfer forms are used, they too must be prepared before the media are stuffed. It should be noted that unit clerks often disregard these requirements for the proper recording of transfers and only stuff the media into the correct accounts. As a result, differences between controls and details are created which are almost impossible to locate. This abuse may, in effect, nullify the effort spent on the recording of the other transfers which are treated properly.

To repeat, misclassification between types of accounts receivable must be recorded under any system if control and general ledger accounts are to be accurately maintained by type of account receivable.

**TRANSFERS BETWEEN CYCLES (MISSORTS)**

Misclassifications of media between cycles require or do not require entries in the control accounts depending upon the timing of the discovery of the error and the type of system in use. In all cases, the media may be used to accomplish the transfer. Missorts fall into three general categories: (1) errors discovered at the time of stuffing, (2) errors discovered at the time of billing which affect an unbilled cycle, and (3) errors discovered at the time of billing which affect a cycle which has been billed.

In the cycle control system, any activity between cycles affects the cycle control balance, so all three of the above types of transfers must be recorded.

Under the two-control system with a daily split of media, an adjustment must be recorded only if both the billed and unbilled control accounts are affected. Thus, transfers of type (2) above need not be recorded since both sides of the transfer remain in the billed
control. Transfers of type (1) above may affect both the billed and unbilled controls and thus may need to be recorded. Items of type (3) above always involve a transfer from the billed to the unbilled control and therefore must be recorded.

Since there are no cycle controls established before billing in either the one-control system or the two-control system with a post list split of media, cycle transfers need not be recorded under these systems.

The problem of recording of cycle transfers, therefore, is greatest in a cycle control system. It is of less significance under a two-control system with a daily split, and it is not involved at all in the one-control system and in the two-control system with post listing.

Most stores properly record transfers between cycles if required by the system used. The recording of transfers between types of accounts, however, is not so universally practiced. In some stores which keep separate control accounts in all other respects, transfers between types of accounts are not recorded. In these cases, differences between details and controls must often be judged, (1) in total for all types of accounts, or (2) by type of account after an arbitrary adjustment of the controls for the estimated amount of the transfers. In the latter case, the adjustment often allows the difference to fall to the 30-day account group. Procedures such as these substantially defeat the purpose for keeping controls by type of account and compound the problem of locating differences. The keeping of separate general ledger and accounts receivable control accounts, therefore, appears to be a very questionable practice especially if transfers between types of accounts are not to be recorded.

The recording of transfers is a difficult and a costly aspect of an accounts receivable control system.
It is, however, an essential procedure if the system is to function properly and the prescribed degree of control is to be maintained.

If one general ledger account and one set of controls are used, there is no problem of transfers between types of accounts. If individual general ledger and control accounts are used, the recording of transfers cannot be avoided if the system is to be fully effective. However, since the keeping of separate general ledger accounts and controls results in more work without measurably improving internal control, and since statistical data such as the aggregate balances for each type of account and collection percentages are available from analyses of billing tape totals, stores are well advised to consider the use of a single general ledger account and control account for all receivables.
GENERAL RULES OF INTERNAL CONTROL PROCEDURES

Within the general framework of each of the basic types of cycle billing control systems, the effectiveness of the internal control will vary widely depending upon the specific procedures adopted by an individual store as a part of its system. Enumerating the more important techniques of internal control for cycle billing should prove helpful. Although some of these are more basic than others, no effort has been made to list them in the order of importance. Also, some of these rules are applicable to billing systems in general, whether or not on a cycle basis.

(1) The fundamental principle of internal control is segregation of duties among employees so that no one person is in complete control of any important part of the business transactions and whereby the work of each employee is checked by another. Accordingly, the control clerk should not independently create any of the figures entered in the controls. In addition to the figures for basic transactions (charges, credits and cash) the control figures for transfers, adjustments, write-offs, etc. are encompassed by this rule.

(2) There should be a periodic, detailed check of the control clerk's functions in order to strengthen the internal control and reduce the possibility of manipulation of control records. This can be accomplished by either of two ways: (a) the substitution of another qualified control clerk for such duration as to allow for a recording and reconciliation of the control figures by the substitute clerk for one month each year, or (b) an extensive examination by the internal auditor of the entries and reconciliation for at least one month each year.

(3) The postings to control accounts should be made in ink, or by machine, on a daily basis and
erasures should be prohibited. Corrections should be made by crossing out and entering the correct hand posted figures, or by the reversing and re-entry of machine figures.

(4) A copy of all control figures submitted to the control clerk should be retained by the originating department (sales audit or cashier) to provide a record for subsequent checking.

(5) The control clerk should retain adequate supporting data for all entries in the control records. In most instances where the figures entered in the control accounts will have been developed independently by another person, this support will consist of the form on which the figures mentioned in (4) above were submitted. If the control clerk develops certain control figures, even though this practice is not recommended, the support should consist of a copy of the original adjusting document or a microfilm record of same. Consideration should be given to the microfilming of missorts (transfers between cycles) if entries in the controls are required by the control system in use. (See section on transfers between cycles).

(6) Records relating to accounts receivable (including those retained in the originating department) (see 4 above) should be kept for a period of at least 18 months. The records retained should include the control accounts, all reconciliations between details and controls or controls and general ledger, billers' trial balance tapes, post listing tapes, daily control totals developed by sales audit or cashier, daily summary of transfers developed by sales audit or transfer clerk, records of cut-off dates, approved lists of accounts written off, microfilm record of customers' accounts and statements, control account for unidentified cash and credits and all other records which are an important part of the accounts receivable control
system. The availability of past records is essential if large differences must be investigated.

(7) The determination of totals of split batches of media by adding the smaller of the two groups and deducting this figure from the total for both groups to arrive at the figure for the larger group should be permitted only if it is certain that adequate physical control over the media can be maintained in this process. Where a large volume of media is involved physical control over the media usually is difficult, and the adding of both batches often is the preferred practice.

(8) The accounts receivable department should verify that the dollar value of media received from other departments agrees with the figures for such media as entered in the control accounts. This verification may be made on a test basis.

(9) Correction of control differences noted by any department receiving media should be approved by the originating department.

(10) All media should show the date the transaction took place or the date of preparation of the document. If validation devices (sales registers, window posting machines, etc.) have a dating feature, steps should be taken to see that they print the correct dates at all times. However, the most important date is the one on which media became a part of the control, and thus all documents should be so dated by the originating department, usually the sales audit department.

(11) The preparation of cash media should be done in a manner which makes alteration of amounts improbable; thus machine validation, or use of indelible pencil and written amounts is important.

(12) If the two-control system with post listing is used, all media should be marked in such a way that the identity of the month they became part of the gen-
eral ledger balance is clear. Color coding, for example, is very difficult to identify on microfilm.

(13) Strict security measures over accounts receivable media and the accounts receivable file area should be in effect to prevent loss from misplacement, deliberate destruction, or misapplication of media. Such measures include the following:

(a) Customers' account files should be located in a separate room or location, or within some type of enclosure which permits access on a basis which can be effectively controlled.

(b) Accounts receivable media should not be left unprotected during non-working hours. All such media in all departments (including sales audit) should be placed in locked files or vaults at night.

(c) Careless waste disposal from accounts receivable and related departments should be avoided. For example, the contents of waste receptacles should be inspected for unbilled media before they are emptied.

(d) Access to the accounts receivable files should be limited to those whose work requires use of the files and should be denied to all others. Cashiers, sales audit clerks and salespeople should be denied access to cycle files. (A corollary to this point is that accounts receivable personnel should not have access to the cash office or participate in handling accounts receivable collections.)

(e) Media should never be taken from the customers' account files. Under properly controlled "out" card systems, perhaps it is permissible to allow ledger cards to be taken, but media

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never should be removed. The out card system for ledger cards should show the name of the account taken, the balance of the account and the name and department of the person taking the account card.

(14) While employee accounts in general constitute a specific area of great exposure the accounts of employees in the accounts receivable, sales audit and cashier's departments comprise the most "vulnerable" group. Positive steps should be taken to provide adequate control. Among the methods being used are:

(a) Physical separation and separate billing, even on a descriptive basis with frequent, almost daily postings.

(b) Distinctively colored statements, or address plate coding, with a special review before being mailed.

(c) Test-checking of activity in these accounts, selected on a rotating basis.

(15) The responsibility for stuffing media in the customers' account pockets should be exclusively that of the unit operators and officially authorized alternates. The stuffing of media of any kind by persons other than those authorized to do so should be prohibited. All media to be filed should be controlled and routed to the unit operator through approved processing channels.

(16) Cash and credit media which cannot be identified with a customer's account should be recorded in a separate record and the details should be balanced periodically to the "unidentified" control account. These separate records (and controls) may be spread throughout the cycle files, such as one to each cycle or more. The media should be clearly marked to
prevent unauthorized use. Upon completion of tracing activity and the writing off of the corresponding balances, the media should be cancelled or destroyed. Transfers out of the "unidentified" accounts to active accounts should be made only on the basis of a form approved by an authorized person after careful review.

(17) All media as well as the customers' statements should be microfilmed upon completion of billing and before mailing.

(18) Statements should be mailed each month for all regular (30 day) and revolving credit accounts. If cycle or another billing system is in use for installment type accounts, monthly statements also should be mailed on this type of account. However, if installment accounts are handled on a coupon or window posting basis, confirmation type statements should be mailed on such accounts at intervals designed to cover an extensive sample thereof each year. The "holding" of statements from mailing should be approved in some manner, such as (a) in the case of temporary holds, by notation and initials of the person so requesting on the face of the statement before microfilming, and (b) in the case of permanent holds, by the insertion of an approved form stuffed in the account pocket before billing and microfilming. The necessity for permanent "holds" should be reviewed and challenged periodically. The mailing of statements and the screening of returned mail (non-deliveries) should be done by personnel other than those of the accounts receivable, credit and cashier's departments, usually by the mailing department.

(19) Since, as previously mentioned, a monthly comparison of billing trial balances and control figures by type of transaction (charges, credits, cash, etc.) is desirable, the billing tape totals for charges, cash, credits, etc. should be "clean" totals and billing corrections should be made in such a manner as to
keep the totals clean. Therefore, uniform procedures of correction should be used by all billers with the correction of one column or register by offset in another being avoided if possible.

(20) A reconciliation of billing trial balances with controls should be made as soon as the necessary figures are available.

(a) Under every control system the total of the pickups of old balances should agree with the total of the closing balances of last month, tray by tray or cycle by cycle.

(b) Under the cycle control system reconciliation should be made as soon as the billing of each cycle is completed during the month, it being understood that at the month end the master control (sum of individual cycle controls) should agree with the general ledger.

(c) Under the two-control system reconciliations should be made as soon as the last cycle of the month is billed, it being recognized that under the two-control post list system this reconciliation relates to media processed for the second preceding month.

(d) Under the one-control system this reconciliation (inventory) ideally should be made once a month. Less frequent inventories or trial balances increase the store's risk proportionately. If the media are photographed before being filed, the risk is modified somewhat although the reconstruction of customers' accounts from this source is difficult and expensive.

Where applicable such reconciliations generally should be made by type of transaction (charges,
cash, credits), especially if the over-all difference between billing totals and control figures is above a predetermined tolerance.

(21) Adherence to predetermined cycle cut-off dates is important in an accurate and orderly cycle billing system. Deviations from established cut-off dates always create a risk, but the risk is greater under some control systems than others. In the case of the two-control system with a prebilling daily split of media, failure to adhere to cut-off dates makes reconciliation between billing totals and controls extremely difficult. The correction of controls depends upon the possibility of re-adding the affected media if they are still unstuffed. Under the cycle control system, amounts representing variations from cut-off dates become reconciling items. Under the two-control system with post listing, variations from cycle cut-off dates do not affect reconciliations unless the shifting of dates results in media from three (instead of two) fiscal months being included in the billing of any cycle.

(22) A permanent record of the actual cut-off dates of each cycle should be provided. This can be accomplished by including as the first item on the microfilm record of each cycle a form showing the cut-off date for each type of media, or it can be entered in ink or indelible pencil in the control records.

(23) The non-print features commonly found on billing machines should be made inoperative to prevent the manipulation of machine totals.

(24) Billing machine operators should not leave a billing machine unattended in the middle of a run for extended periods of time without taking steps to see that unauthorized entries are not made thereon. Such steps could include clearing the machine by total or subtotal, or initialing the tape at the point of last entry.
(25) Care should be exercised to assure a microfilm record of high quality because after customers' statements are mailed, the only existing record of the transactions in those accounts is the microfilm record of the billed media. Clarity of focus and the absence of overlapped media are important.

(26) The existence of uncancelled cash and credit media presents the possibility of altering such media re-entering into the files to obtain fraudulent credit. All cash and credit media should be cancelled after billing, whether or not it is mailed to customers. This can be accomplished by the use of an inked wheel on certain makes of microfilm equipment, by perforation, or by any other effective device.

(27) If cash media applicable to zero balance or credit balance statements are not to be mailed to customers, they should be extracted and destroyed under the supervision of the accounts receivable or billing supervisor. If the procedures provide that no cash media on any account are to be mailed to customers, all such media should be destroyed under proper supervision.

(28) Write-off of customers' accounts should be made only on the basis of an authorized list or other record, showing names and amounts, and signed by the head of the collection department or the credit manager. The entry to the control account for write-offs should be prepared by the credit department and copies should be forwarded to the accounts receivable control clerk and the general ledger clerk. The routine write-off of small balances should be approved in total.

(29) "Active" P & L accounts should be physically segregated and a separate memorandum control maintained. A trial balance of these accounts should be taken periodically and balanced to the memorandum
control account. Statements should be mailed at intervals (once or twice a year) to all active P & L accounts, including those in the hands of outside collection agencies, or confirmation of payments (or lack of payments) should be mailed on such accounts.

(30) Allowances and similar adjustments should be adequately approved. Such approval should originate outside the accounts receivable department.

(31) When the billing for a particular cycle has been completed, some media often remain on hand which, for various reasons, were not included in the billing. Constant efforts should be exerted to keep these "throw-outs" to a minimum. Depending upon the particular control system in use, throw-outs may become reconciling items in the comparison of billing balances with control account balances. In order to provide a proper record to support these reconciling amounts, all throw-outs should be microfilmed at the completion of the billing for the cycle.

(32) In some stores, charge sales procedures do not provide for other than the original salescheck which should become the charge to the customer's account. Every store should carefully evaluate this risk. The magnitude of the risk involved in not having an extra copy of the salescheck is related to the length of time before significant differences between billed detail and accounts receivable controls are determined. This time period is computed from the point at which the sales check is written or at which control figures are established (the audit date of the media) to the point indicated below:

One-control system - To the end of the first or to the end of the twelfth month after the billing of the cycle, depending upon when the inventory is taken.
Cycle control system - To the completion of the billing of each cycle.

Two-control system with daily split of media - To the end of the month in which the account is billed.

Two-control system with post list of media - To the end of the month subsequent to the month in which the cycle is billed.

In all situations, accounts cannot be reconstructed if saleschecks are fraudulently destroyed at any point before billing.
EXHIBIT A

SUMMARIZED ADVANTAGES AND DISADVANTAGES
OF CONTROL SYSTEMS

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>One-control system</td>
<td>1. The taking of physical inventory of loose media in the customers' files creates a tremendous peak work load. This system is, therefore, more adaptable to smaller stores where the number of accounts is not great.</td>
</tr>
<tr>
<td>1. This is the only control system whereby the existence and the total dollar amount of all loose media in the customers' account files are firmly established at one date.</td>
<td>2. The margin of human error in the inventory results may be large enough to nullify the effectiveness of this procedure as a control device.</td>
</tr>
<tr>
<td>2. This is the only control system whereby the total actual difference between the details of all the customers' accounts and the general ledger balance is known at one date.</td>
<td>3. When a large difference is disclosed, there is no way of knowing in which letter of the alphabet to begin to look for the cause.</td>
</tr>
<tr>
<td>3. This is the only system under which accounts receivable control accounts are not required. No clerical activity is required for daily posting of control accounts or the recording of transfers for missorts between cycles. There may be some savings in not having to set up control figures in sales audit.</td>
<td></td>
</tr>
</tbody>
</table>
Advantages

Cycle control system

1. This is the only system which provides individual control over small segments of the accounts (cycles) and allows a determination of the difference between billed detail and accounts receivable controls to be made immediately upon the billing of a cycle.

2. This is the only system under which the accounts receivable control account balances can be tied in to the general ledger at any date during the month.

Disadvantages

1. Under this system cycle control accounts must be maintained. Clerical activity is, therefore, required to develop original control totals in sales audit, post to the control accounts daily and adjust the control accounts for original misclassification of media by cycle.

2. The cycle control system is especially susceptible to manipulation by "lapping" through the recording of fictitious temporary transfers between cycles.

3. Unless cycle differences are rigorously pursued the potential benefits of this system are not gained. If differences in one cycle are considered as being offset by differences in other cycles, a cycle control system is not actually in effect.
Advantages

Two-control system with a pre-billing daily split of media

1. Compared with the cycle control system, a smaller number of control accounts are maintained. As a result there is less clerical activity in that fewer control totals must be developed each day in sales audit, fewer postings must be made each day to control accounts, and only a portion of the missorts between cycles need be reprocessed and recorded as adjustments to the control accounts.

Disadvantages

1. Differences are not finally determined until the end of the month following the month of billing, although there is a reconciliation at the end of the current month using the computed figure of unbilled media.

2. Control figures and differences are in total only for all cycles. Compared to the cycle control system, differences are much more difficult to locate.

3. Control of any deviation from an absolute adherence to cut-off dates is extremely difficult under this system. Since control totals are developed daily based on predetermined cut-off dates and are in total for all cycles, errors in original determination of control figures are impossible to locate after media are stuffed. The billing of a cycle as of any date other than the fixed cut-off date automatically creates a difference between details and controls which, because it cannot be evaluated, negates the value of the "unbilled" control balance at the end of the month. However, since changes in cut-off dates usually result from delays in processing media into the files, it may be possible to reconstruct the totals by re-adding the unstuffed media involved in the change.
Advantages

Two-control system with a post list split of media

1. Compared with the cycle control system and the two-control system with a pre-billing daily split of media, only the simplest of control records are required to record the post list totals.

2. Compared with the cycle control system and the two-control system with a pre-billing daily split of media, clerical time is saved by not being required to develop control totals in sales audit, post predetermined figures to accounts receivable control accounts and adjust control accounts for missorts between cycles.

3. This is the only system which provides a complete re-examination and totaling of each type of media billed.

Disadvantages

1. Control totals cannot be developed or differences determined until after the end of the month following the month of billing. Since control totals under this system are established after the billing of each cycle, there is no provision for a reconciliation to the general ledger at the end of the current month using computed figures for unbilled media, such as is possible under the cycle control system and the two-control system with a pre-billing daily split.

2. Control figures and differences are in total only for all cycles. Compared to the cycle control system, differences are much more difficult to locate.

3. By its nature, this system forces a post list operation, the cost of which may offset much of the saving mentioned as an advantage.