

What are Internal Controls?

Worksheet

Internal controls are the processes and safeguards a business uses to protect its assets, ensure accurate accounting records, and prevent or catch errors and fraud.

Questions

1. Which is an example of a preventive control?
 - A) Bank reconciliation
 - B) Requiring two signatures on large checks
 - C) Annual inventory count
 - D) Reviewing variance reports
2. A monthly bank reconciliation is what type of control?
 - A) Preventive
 - B) Detective
 - C) Corrective only
 - D) Not a control
3. What is the main goal of internal controls?
 - A) Maximize revenue
 - B) Safeguard assets and ensure accurate records
 - C) Reduce employee headcount
 - D) Set stock prices
4. Segregation of duties means
 - A) One person handles a task start to finish for speed
 - B) Different people handle related tasks to reduce fraud risk
 - C) Only managers can touch the books
 - D) Duties rotate randomly with no plan
5. A \$10,000 wire transfer requires sign-off from both the controller and the CFO before it is sent. What type of control is this, and why?
6. At month-end, the bookkeeper compares the bank statement balance of \$42,300 to the company's cash ledger balance of \$41,950 and investigates the \$350 difference.
7. A retail store counts its physical inventory every quarter and compares it to the \$150,000 recorded in the accounting system.
8. Define: What is an internal control?
9. Define: Preventive vs. detective control?
10. Define: What is segregation of duties?

Answer Key

1. B) Requiring two signatures on large checks - Dual signatures stop unauthorized payments before they happen - that's preventive.
2. B) Detective - It finds discrepancies after transactions occur, so it's detective.
3. B) Safeguard assets and ensure accurate records - Internal controls protect assets and support reliable financial reporting.
4. B) Different people handle related tasks to reduce fraud risk - Splitting related duties among different people creates checks and balances.
5. This requires two people to approve before the transaction happens It's a preventive control (segregation of duties / dual authorization) It reduces the risk of one person committing fraud undetected
6. This comparison happens after transactions are recorded It's a detective control (bank reconciliation) The \$350 gap is traced to an outstanding check, confirming no fraud or error
7. The count happens after goods have already moved in/out It's a detective control (physical inventory count) Any difference from the \$150,000 book value signals theft, damage, or recording errors
8. A policy or procedure that protects assets and ensures accurate financial records.
9. Preventive controls stop errors/fraud before they happen; detective controls find them after.
10. Splitting a task (like approving and recording a payment) between different people to reduce fraud risk.

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