UNIT-4

VOUCHING OF CASH TRANSACTIONS

Vouching of cash receipts

Opening Balance of Cash Book

Opening balance of cash book represents cash in hand at the start of the year and should verified from the balance sheet of last financial year.

Cash Received from Debtors

Consider the following points for verification of cash received from debtors −

- The carbon copies or counterfoils of cash receipt book should be verified.
- Cash receipt should be serially numbered.
- Cash received should be entered on the same date when the cash is actually received.
- The discount allowed to customers should be properly authorized by a responsible officer.
- Correspondence with customer and ledger account should be tallied.

Following are the different ways used for misappropriation of cash −

- Cash received from customer not recorded in books and no cash receipt may be issued.
- Issuance of receipt for lesser amounts than amount actually received.
- Using **teeming and lading** method; it is a very common method to misappropriate the money, in which the cash received from any customer not recorded in the books and the cash received from same customer at a later instance or another customer recorded in the books and so on.

Repayment of Loan by Others

Repayment of loan by others may be verified in the following ways −

- Calculation of interest received and interest should be credited to interest received account.
- Verification from bank statement if directly deposited by party into bank.
- Checking of carbon copies or counterfoils of cash receipts.
- To ensure that there should be no violation of Income Tax rules as payment of loan exceeding Rs. 20,000/- cannot be repaid in cash. It should be through Cheques, Demand Draft, NEFT, RTGS or any other available banking channels.

Rent Received

- To check rental agreement or lease deed.
- In case where the rental income is received from more than one property, separate account for each property should be maintained.

- The Auditor should verify that the rent for all the twelve month is received or not.
- The amount of rent should be verified from the rent deed or the lease deed.
- If TDS (Tax Deducted at Source) is deducted by the party, there should be proper accounting of TDS.

Sale of Investments

- To check bank statement if the sales proceeds have reached the bank account.
- To verify broker commission, note or debit note, if investments are sold through broker.
- To ensure separate accounting is being done for capital receipts and revenue receipts. Dividend or profit or loss on sale of investment is a revenue receipt and the sales proceeds of the investment cost should be booked as capital receipt.

Subscription

Subscriptions are received from the members of a club and the following points need to be considered by the Auditor while vouching subscription −

- Subscription register should be verified.
- Verification of subscription received during the year and the subscription receivable.
- Counterfoil of cash receipt should be verified.

Sale of Fixed Assets

- To check minutes of the meetings of the Board of Directors.
- Sale agreement or sale contract.
- Verification of agent account if sale is made through an agent.
- Profit or Loss on sale of fixed assets should be booked to revenue account.
- Authorization of sale of fixed assets.
- Sale proceed of fixed assets should be credited to fixed assets account after deducting expenses on sale of fixed assets if any.

Interest and Dividend Received

- Verification of the dividend warrant letter along with the covering letter for verification of dividends in case of dividends received through cheque.
- Verification of bank statement, if the dividend is directly credited to the bank account.
- Interest on security can be vouched from the securities schedule.
- Interest on fixed deposit can be verified from bank statement and TDS certificates.
- Interest received from outsiders to whom company has granted loan could be verified from statement of account of party along with TDS certificates.
- Provision should be made for interest accrued but not due.
- All interest received and accrued should be properly accounted for in the books of accounts.

Commission Received

- Verification of agreement on the basis of which the commission is received.
- Calculation of the commission receivable.
- The commission received should be verified from counterfoils, bank statements, cash receipts, etc. and the provision for commission receivable should be rightly accounted for in the books of accounts.
- Commission receivable on "sale of goods sent on consignment" should be verified from sale account.

Installments Received on Hire-Purchase Sale

- Study of the Hire-Purchase agreement for hire-purchase-sale price, number of installment, rate of interest etc.
- Segregation of principle amount and interest amount should be done and both should separately account for.
- Profit on sale on hire-purchase should be duly calculated on the basis of installment received during the year.

Vouching of Cash Payments

All the payment made to creditors, expenses incurred in cash and all other payments done appear on the credit side of cash book and the Auditor is required to vouch cash payments because chances of cash misappropriation are very high.

Following points need to be considered for different types of cash payment −

Opening Balance

The opening balance of cash book can never be credited because cash of company cannot be in negative but the credit bank balance represents the overdraft account from bank or utilization of cash credit limit as sanctioned from bank.

Payment to Creditors

Payment to creditors may be examined by the following −

- Receipt issued by the creditors.
- If the creditor is paid amount as full and final settlement, the balance amount, if any stands in the ledger account of the creditor; this amount should be credited to discount received.
- If any advance payment is made to creditor that should be clearly mention.
- Statement of account of creditor.

Payment of Salaries

Depending upon the adequacy of internal control system in an organization Auditor will decide his audit Program. It is very important for Auditor to check the following −

- Attendance record of employee and salary register.
- Appointment letter of new employees.
- Comparison of current month salary with last month’s salary and if there is any abnormal change in amount, Auditor should verify the same.
- Alteration in amount of deductions on account of advance, loan, fine, funds, insurance, TDS, etc.

Payment of Wages

At the time of vouching of wages paid, the Auditor should verify the following points to avoid misappropriation of cash −

- Adequacy of Internal Control System.
- Payment of wages at higher rate than allowed.
- Payment shown to ex-workers in the current month.
- Lower or non-deduction of advance or other deductions due.
- Payment to fictitious workers.
- Payment to workers who were absent from duty.
- Wages sheet should compare with wages register.
- Comparison of current month wages with last month’s wages and proper verification should be there for extra ordinary changes.
- Detailed verification for payment to casual workers.
- Vouching and verification of treatment accounting treatment for unpaid wages.

Purchase of Plant and Machinery

The Auditor should pay attention to the following −

- Purchase invoice of machinery.
- Freight inward charges, installation charges, erection and commissioning charges should be capitalized.
- Treatment of Excise duty according to the excise rules.

Purchase of Land & Building

Purchase of Land and Building can be vouched as follows −

- Study of Lease hold agreement, if land is purchased on lease hold basis.
- Payment should be as per lease term.
- All the expenses incurred to acquire lease hold property should be debited to respective property account.
- Auditor should study the conveyance deeds in case property is purchased under free hold basis.
- For verification of payment, the Auditor can check the payment receipt and the conveyance deed.

Rent Paid

Consider the following points for the verification of rent by the auditor −

- Rent Deed.
- Rent receipt from Land lord.
- Provision for un-paid rent at the end of the year.

Insurance Premium

Consider the following points for the verification of Insurance Premium −

- Insurance policy issued by the Insurance Company.
- Insurance premium receipt
- Insurance premium should not be related to any official of the company.

Income Tax

Consider the following for the verification of Income −

- Advance Tax Challan
- Self-Assessment Tax challan
- Income Tax demand notice
- Assessment order

Excise Duty

Consider the following for the verification of Excise Duty −

- Rate of Excise Duty
- Excise records and sale invoice for verification of excise duty

Commission on Sale

Consider the following for the verification of Commission on Sale −

- Agreement of sale.
- Rate of commission on sale.
- Calculation of commission on the basis of sale.
- Cash receipt issued by agent.
- Provision for commission payable

Director’s Fees

Consider the following for the verification of Director’s Fees −

- Directors receive fees for attending the Board meetings.
- Verification of attendance register.

- Verification of payment receipt duly acknowledged by the directors.

Internal Control System for Cash Transactions

Following are the main features of a good internal control system −

- All cash received should be accounted for immediately.
- All received cheques should be crossed immediately on receipt.
- Cash receipt should be issued to debtors and daily reconciliation of account should be done where the debtors pay cash on daily basis.
- All cash receipts should be deposited in bank on a daily basis.
- Bank reconciliation account should be prepared on a regular basis.
- Payments other than petty payments should be done through crossed cheques.
- Cash receipt should be obtained for every cash payment to creditors.
- Cash expenses should be duly supported by proper and genuine bills or vouchers.

UNIT-5

Verification

Meaning

Verification means the act of assuring the correctness of value of assets and liabilities in the organization. It refers to the examination of proof of title and their existence or confirmation of assets and liabilities on the date of Balance Sheet. It usually indicates verification of assets of any organization, which can be done by examination of values, ownership, existence, possession of any assets and also ensures that the assets are free from any charge. In simple words, verification means, ‘proving the truth or confirmation’.

Definition

Spicer and Pegler defines Verification as, “An inquiry into the value, ownership and title, existence and possession and the presence of any charge on the asset”.

Auditor’s Duty Regarding Verification

The auditor of a business is required to report in concrete terms that the Balance Sheet exhibits a true and fair view of the state of its affairs. In other words, he has to examine and ascertain the correctness of the money value of assets and liabilities appearing in the Balance Sheet and this examination is known as verification of assets and liabilities. Therefore, an auditor has to keep in mind the following points while verifying the assets:

- Ensuring the existence of assets.
- Acquiring the assets for business.
- Legal ownership and possession of the assets.
- Ensuring the proper valuation of assets.

VALUATION

Meaning

Valuation means finding out correct value of the assets on a particular date. It is an act of determining the value of assets and critical examination of these values on the basis of normally accepted accounting standard. Valuation of assets is to be made by the authorized officer and the duty of auditor is to see whether they have been properly valued or not. For ensuring the proper valuation, auditor should obtain the certificates of professionals, approved values and other competent persons. Valuation is the primary duty of company officials. Auditor can rely upon the valuation of concerned officer but it must be clearly stated in the report because an auditor is not a technical person. Without valuation, verification of assets is not possible.

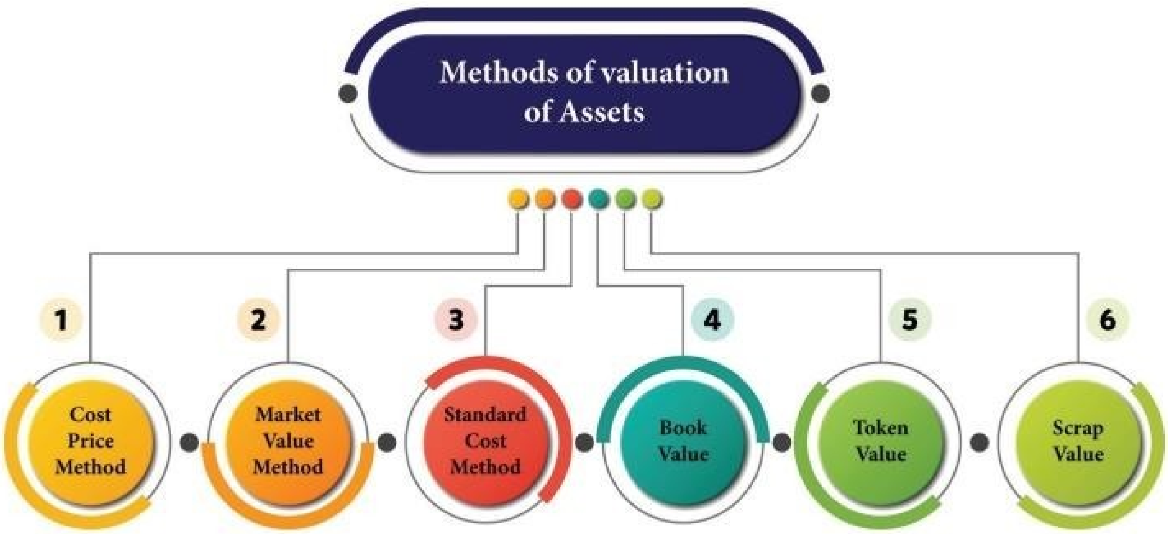
If the valuation of assets is not correct, both the financial statements such as Balance Sheet and Profit and Loss Account cannot be correct. Hence, the auditor must take utmost care while valuing the assets to show true and fair view of the state of affairs of the financial position of the concern.

Definition

R.Batliboi, "A company's Balance Sheet is not drawn for the purpose of showing what the capital would be worth if the assets were realized and liabilities paid - off, but to show how the capital stands invested".

Methods Of Valuation

Valuation of various assets can be made by using different methods of valuation of fixed assets. Some of the major methods are as follows:



1. Cost Price Method

In this method, valuation of assets is made on the basis of purchase price of the assets. This price refers to the price at which an asset is acquired plus expenses incurred in connection with the acquisition of an asset. It is a very simple method of valuing assets.

2. Market Value Method

Valuation of assets can be made on the basis of market price of such assets. But if same nature of assets is not available in the market, it is very difficult to determine the value of such assets. So, there are two methods related to it. They are:

i. Replacement Value Method

It represents the value at which a given asset can be replaced. This method of valuation of assets can be done only in the case of replacement of the same asset.

ii. Net Realizable Value

It refers to the price in which such asset can be sold in the market. But expenditure incurred at the sale of such asset should be deducted.

3. Standard Cost Method

Some of the business organizations fix the standard cost on the basis of their past experience. On the basis of standard cost, they make valuation of assets and present in the Balance Sheet.

4. Book Value

This is the value at which an asset appears in the books of accounts. It is usually the cost less depreciation written off so far.

5. Going concern or Historical Value or Conventional Value or Token Value

It is equivalent to the cost less a reasonable amount of depreciation written off. No notice is taken of any fluctuation in the price of the assets. Reason for this is that these assets are acquired for use in the business and not for resale.

6. Scrap Value

This method shows the value realized from sale of an asset as scrap. In other words, it refers to the value, which may be obtained from the assets if it is sold as scrap.

Auditor’s Duty as Regards Valuation

In a legal case against Kingston Cotton Mills Co: It was held that “although it is no part of an Auditor's’ duty to value the assets and liabilities, yet he must exercise reasonable skill and care in scrutinizing the basis of valuation. He should test the accuracy of the values put by the officers of the business. In any case, the auditor cannot guarantee the accuracy of the valuation”.

It is not an auditor's duty to determine the values of various assets. It has been judicially held that he is not a valuer or a technical man to estimate the value of an asset. But he is definitely concerned with values set against the assets. He has to certify that the profit and loss account shows true profit or loss for the year and Balance Sheet shows a true and fair view of the state of affairs of the company at the close of the year. Therefore, he should exercise reasonable care and skill, analyse all the figures critically, inquire into the basis of valuation from the technical experts and satisfy himself that the different classes of assets have been valued in accordance with the generally accepted assumptions and accounting principles. If the market value of the assets are available i.e., in the case of share investment then he should verify the market value with the stock exchange quotations. If there is any change in the mode of the valuation of an asset, he should seek proper explanation for it. If he is satisfied with the method of valuation of the assets, he is free from his liability.

Differences Between Verification and Valuation

S. No.	Basis	Verification	Valuation
1.	Meaning	Verification establishes existence, ownership and acquisition of assets.	Valuation certifies correctness of the value of assets and liabilities.
2.	Evidence	The title deed, receipt for payments constitutes documentary evidence for verification.	The Certificate offered by the owner or directors or experts is the documentary evidence for valuation.
3.	Checking	The auditor is required to verify whether the value ascertained is fair one or not.	Critical examination of the value of assets and comparative analysis of different assets.
4.	View	Verification includes apart from valuation, the examination of ownership right, the existence of the asset in the business and its freeness from any sort of charge.	Testing the exact value of an asset on the basis of its utility.
5.	Work	Verification is a final work.	Valuation is the initial work and it need to be verified subsequently.
6.	Personnel	Verification is the work of auditor.	Valuation is the work of concerned authority or board(company).
7.	Time	Verification is made at the end of the year.	Valuation is made throughout the year.

AUDIT REPORT

An audit report is a written opinion of an auditor regarding an entity's financial statements. The report is written in a standard format, as mandated by generally accepted auditing standards (GAAS). GAAS requires or allows certain variations in the report, depending upon the circumstances of the audit work in which the auditor engages.

An audit report is issued to the user of an entity's financial statements. The user may rely upon the report as evidence that a knowledgeable third party has investigated and rendered an opinion on the financial statements. An audit report that contains a clean opinion is required by many lenders before they will loan funds to a business. It is also necessary for a publicly-held entity to attach the relevant audit report to its financial statements before filing them with the Securities and Exchange Commission.

Contents or Elements of Auditor's Report

The report of a certified auditor or auditors stating the accuracy of financial statements of a public limited company is known as auditor's report. This report is a written letter from the auditor containing the view of whether a company's financial statements observe with generally accepted accounting principles (GAAP).

The content of an Auditor's Report needs to be clear and accurate, providing enough verification to validate the auditor's estimation. The auditor's report should incorporate the following elements:

- **Title:**

The auditor's report should contain a heading as styled "Auditor's Report."

- **Addressee:**

Every auditor's report must address the recipients or readers of the report. State the party, such as the limited management or shareholders, to whom the report is addressed.

- **Introductory Paragraph**

In the introductory paragraph, the names of the financial statements audited should be provided. This generally includes the profit and loss account, balance sheet, cash flow statement, statement of changes in equity and other accommodating books that were used in the preparation of financial reports.

- **Identification of the financial statements audited:**

In the report, the auditors should specify the name of financial statements audited by them during the financial year. They generally audit profit and loss statements, balance sheets, cash flow statements, and ounces equity statements. All other supportive books of accounts are also within the purview of their audit.

- **Management Responsibilities:**

After Addressee the liability towards the financial statement is to be written which includes the responsibility of management towards the research and arrangement of financial statements.

- **Auditor’s Responsibility:**

After management responsibility auditor’s liability is to be written which includes their accountability to matter an impartial estimation on the financial statements.

- **A reference to the auditing standards and practices followed:**

The auditors follow certain generally accepted accounting standards. Here they specify the standards followed by them in auditing. In this section, the Auditor clearly mentions that it is the accountability of the administration or board to organize the financial statements and preserve internal controls.

- **Expression of opinion on the financial statements:**

On the basis of the fact of the audit, report opinion is to be stated. They must give a declaration stating whether the statements and books of accounts represent a true and fair view of company affairs. Then the auditor is essential to write his own audit report opinion on the reality and sprite of the financial statements specifying the foundation of such opinion.

- **Signature:**

At the end of the report, they need to put their signature. Example – The signature is to be done by the appointment collaborator of the audit firm and below that the name of the appointment partner and the audit firm is to be written.

- **Auditor’s address:**

The full name and address of the audit firm are to be mentioned in the report.

- **The date of the report**:

Every report must mention the date on which it was prepared and submitted.

Types of Audit Reports

Here are the four types of audit reports that are given by external auditors:

1. **Unqualified Opinion**

   If your company gets this opinion, that's a good thing. An unqualified opinion indicates that the information presented in a company’s financial report is clean. An unqualified opinion shows that the audited financial statements can be presumed to be free from misstatements.

2. **Qualified Opinion**

   An opinion rendered in a qualified audit report is similar to an unqualified opinion; however, the auditing body cannot express an unqualified opinion for several reasons. One reason could be that the company did not present its financial records in accordance with GAAP.

3. **Disclaimer Opinion**

   Auditors give a disclaimer when they are unable to express a definite opinion. This can be due to the lack of properly maintained financial records or the absence or insufficient support from the management. For instance, an auditor may not have had the opportunity to fulfill tasks that they deem to be crucial to the audit, such as observing operational procedures or reviewing particular procedures.

4. **Adverse Opinion**

   When auditors issue an adverse opinion, it indicates that there has been a gross misstatement and, possibly, fraud, in the preparation of the company's financial records. An adverse opinion shows that the company's records have not been prepared in accordance with **GAAP**. Financial statements with adverse audit opinions are typically rejected by financial institutions or investors.