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SYLLABUS:

VERIFICATION AND VALUATION OF ASSET AND LIABILITY – Auditors Position – Auditors Duties Regarding Depreciation, Reserves and Provisions

MEANING

Verification means proving the correctness. One of the main works of auditor is verification of assets and liabilities. Verification is the act of assuring the correctness of value of assets and liabilities, title and their existence in the organization

DEFINITION

According to **Spicer and Pegler** "The verification of assets implies an inquiry into the value, ownership and title, existence and possession, the presence of any charge on the assets.

OBJECTIVES OF VERIFICATION OF ASSETS & LIABILITIES

1. **Valuation of assets & liabilities**: The auditor has to ensure that the assets & liabilities have been shown at their correct value.
2. **Finding out the ownership & title of the assets**: Verification certifies the ownership & the title of the assets shown in balance sheet.
3. **Detection of errors & frauds**: Verification helps in detecting the frauds & errors in the account books of the undertaking.
4. **Certification of the arithmetical accuracy in account books**: Verification certifies the arithmetical accuracy of the account books
5. **Whether balance sheet exhibits a true & fair financial position of the concern**: Verification helps the auditor to certify the fact whether the balance sheet exhibits a true & fair financial position.

SIGNIFICANCE OF VERIFICATION

The most important duties of an auditor in connection with the audit of the accounts of a concern is to verify the assets and liabilities appearing in the balance sheet.
The auditor should pay a surprise visit and actually count the cash in hand to prevent the cashier to borrow money and make up the deficiency which was due to the past.
To prevent the fraud, the auditor will do well to get a certificate regarding the balance at the bank directly from the bank.
So verification is required to present company's true and fair information.

MEANING OF VALUATION

The process of determining the value of an asset or company. There are many techniques for valuation, and it is often partially objective and partially subjective.
The valuation of assets is therefore an attempt to ensure the equitable distribution of the original outlay over the period of the assets usefulness."

OBJECTS OF VALUATION

a) To know the actual financial position of the company.
b) To know about the goodwill of the concern.
c) To know the difference in the value of assets at the time of purchase & at the date of Balance Sheet.
d) To know the original cost of the assets.
e) To know the mode of investment of the capital of the company

DIFFERENCE BETWEEN VALUATION AND VERIFICATION

Meaning:

Verification means checking whether the assets shown in the balance sheet are in the name of business, whether they exist or not, whether there is any charge on it etc.
Valuation means determining the proper values of assets and liabilities shown in the balance sheet

A. Nature of Work:

Verification examines the assets & liabilities shown in balance sheet,
Valuation examines the entries relating to the transactions recorded in the account book.

B. Time:

Verification is made at the end of the financial year.
Valuation is done for the whole year's transactions.

C. Purpose

The purpose of verification is to check existence, ownership and possession of assets.
The purpose of valuation is to determine the proper values of assets as per generally accepted principles.

D. Basis:

The basis of verification is the type of assets, and liabilities. There is not fixed method of verification.

The basis of valuation of assets is the types of assets are valued on different basis.

E. Personnel:

Verification is done by auditor himself or his assistant ,whereas **Vouching** is done by juniors like audit – clerk .

F. Certificate

The auditor is not able to get certificate of **verification** of assets and liabilities.

The auditor is entitled to get certificate of **valuation** of assets from responsible officer of the business unit.

G. Vouching

Verification includes vouching.

Valuation does not include vouching.

H. Scope

The scope of **verification** is wide. It includes checking of many things like existence, ownership, possession etc.

The scope of **valuation** is limited. Here only values of assets and liabilities are determined and checked.

METHODS OF VALUATION OF ASSETS

1.Replacement Value
2. Market Value
3. Book Value
4. Realizable Value
5. Scrap Value

VERIFICATION & VALUATION OF ASSETS

A) Goodwill

Good will is an intangible asset, therefore it can be verified from records only & it can’t be verified physically, as per accounting standard 10, goodwill shall be recorded in the books only when some consideration in money or money’s worth has been paid for it.

The amount of goodwill is calculated at the time of admission, retirement & death of a partner in the partnership firm.

b) Plant & Machinery

The auditor should examine the plant & machinery from plant register.
It gives full information about the description, cost, provision for depreciation etc.
If the machines are purchased in the current year, the agreement with the vouchers should be verified.
He should see that plant & machinery are shown in Balance sheet.

c) Investments

He should compare the schedule of each investment & securities with the register of investments maintained by the client.
If the investment is made & registered in the name of any other person as a nominee of the company.
He should see that the investment is over valued at a higher price than the cost.

D) Patent Right:

The patent rights should be verified with the certificates granting such rights.
The auditor should also examine the last renewal payment certificate.

E) Trade Marks

A trade mark is examined with the help of assignment deed & the auditor also see that they are registered in the name of client.

F) Bills Receivable:

The balance of the Bills Receivable Account in impersonal ledger will represent bills in hand at the date of Balance Sheet.
During verification auditor should ensure that they are properly drawn, stamped & not overdue.

VERIFICATION & VALUATION OF LIABILITIES

Capital:

The auditor should verify the memorandum of association, articles of association, cash books, pass book & directors minutes book to find out the amount received from shareholders.

ii)Outstanding expenses:

The auditor should get a certificate from a responsible official to see that all expenses for the current year are included and that the payment for each expense such as interest, discounts, salaries, wages, legal expenses, which have not been paid are included.

iii) Creditors:

- The auditor should obtain a schedule of creditors from the client & check the purchase ledger, credit notes etc.
- Certificate should be obtained from the responsible official that all the liabilities accrued at the end of the year.

iv) Bills Payable:

The auditor should vouch the bills with the entries in the cash book

He should reconcile the total of the schedule of bills payable outstanding with the balance in the Bills Payable Account.

v) Contingent Liabilities:

A contingent liability is possible liability of a presently determinable or undeterminable.

which has arisen from past dealings that may not become a legal obligation in the future.

POSITION OF AUDITOR

- Representative of the shareholder
- As on officer of the company
- As a servant of the company
- As agent of the company
- As an agent of outsiders

AUDITORS DUTY REGARDING DEPRECIATION

1. A company can adopt different methods for different type of assets provided that the methods are adopted consistently over the years.

2.The difference of amount of depreciation as charged with old rate and the amount calculated from new rate should be debited to profit and loss account in case of loss.

3.According to schedule II of the companies act, if assets is sold or discarded during the year, depreciation will be charged on pro-rata basis up to date of sale or discard.

4. Account must disclose method of depreciation.

5. Depreciation must be according to provisions of companies act and income tax act.

6. Depreciation should be charged on revalued amount, if there is revaluation of assets.

RESERVES AND PROVISIONS

Reserves

It is created by debiting the profit and loss appropriation account.

It is created to meet an unknown liability, or to strengthen the financial position of the company or for equalization of dividends etc.

A reserve is created only when there is profit in the business.

It can be distributed among shareholders as dividend.

The reserve is created without taking into consideration the actual amount required except in the case of redemption of debentures when a definite sum is set aside.

Creation of reserve depends upon the financial policy of the business and discretion of its management.

It is usually shown on the liability side of the balance sheet as it is not a specific reserve.

Provisions

It is created by debiting the profit and loss account.

It is created to meet a known liability or a specific contingency, e.g.. provision for bad and doubtful debts, or provision for depreciation etc.

A provision is created irrespective of whether there is profit or loss in the business.

- It is not available for distribution as dividend among shareholders.
- A provision is made for a definite amount and, therefore, a definite sum is set aside every year to meet the known contingency.
- Making of a provision is a must to meet known liability or contingency.
- The provision is generally shown on the assets side of the balance sheet.

TYPES OF RESERVES

REVENUE RESERVE:

Those reserves which are created out of profits available for distribution by way of dividend. These may be classified as:

GENERAL RESERVE:

Reserve, which not created for any specific purpose.

eg: general reserve,contingency reserve.

SPECIFIC RESERVE:

Reserve, which is created for specific purpose

Eg: Dividend equalization reserve, debenture redemption reserve.

CAPITAL RESERVE

These reserves created out of profits of capital and not out of operating profits.

Eg: profits prior incorporation, premium on issue of shares and debentures, profit on sale of fixed assets,

Revenue reserve are free for distribution by way of dividend whereas amount of **capital reserves** are not free for distribution by way of dividend.

Books referred:

1.Practical Auditing by B.N.Tandon

2. Principles and practice of auditing by Saxena