Unit II : Vouching, Verification & Valuation

Unit II :- Vouching - Meaning, Need & Importance, Vouching of Cash & Credit transact, Verification & Valuation of Assets & Liabilities

1.MEANING OF VOUCHER

Voucheris the documentary evidence in support of transactions entered in the books of accounts.For every entry in the books of accounts, there should be a voucher supporting it. Receipt, invoice, cash memo, debit note, credit note, account sales, correspondence, counter-foils of cheque book & pay-in-slip, bank pass book, dividend warrant, wage sheets, agreements, a copy of purchase order, material requisition, minutes, resolutions are some of the important vouchers.

1.1 DEFINITION OF VOUCHING

In simple words, vouching means verification of accuracy, authority and authenticity of transactions that appear in the books of original entry with the help of vouchers of these transactions.

We shall examine some definitions of vouching given by different authors:

(1) **According to B.B. Bose:** "By vouching is meant the verification of the authority and authenticity of transactions as recorded in the books of accounts."

(2) In the words of **Ronald A. Irish,** "Vouching is a technical term, which refers to the inspection of documentary evidence supporting and substantiating a transaction."

(3) **De Paula** writes, "Vouching means the inspection of receipts with the transactions of a business together with documentary and other evidence of sufficient validity to satisfy an auditor that such transactions are in order, have been properly authorized and are correctly recorded in the books."

1.2 CHARACTERISTICS OF VOUCHING

The following characteristics of vouching are clear from above mentioned definitions:

(1) It is an examination of entries in books of accounts.
(2) Such examination is done with the help of vouchers like receipts, invoices, counterfoil or cheque books & pay-in-slips, pass-book, agreements, resolutions, minute book, correspondence etc.
(3) Vouching substantiates a transaction.
(4) It ensures the correctness of transactions entered in the books.
(5) It is an important aspect auditing.
(6) Auditor begins his audit-work with vouching.

1.3 OBJECTS OF VOUCHING

The principal objects of vouching are as under:

(1) To see that all transactions correctly recorded in the books of accounts.
(2) To see that entries recorded in the books of accounts are supported by documentary evidence.
(3) To ascertain that all transactions are duly authorized.
(4) To ascertain that no transaction is left out from being recorded.
(5) To see that necessary vouchers relating to entries recorded in books are with the client.

Thus the purpose of vouching is not merely to verify that the payments have been made, but to verity further that the payment relates to the business and is approved by proper authority.

1.4 IMPORTANCE OF VOUCHING

Vouching is the first step for auditing. The auditor commences his work with the examination of entries and vouching plays an important role in this respect. The correctness of books of accounts is tested by vouching. If the vouching is carried out with due care and intelligence, the audit work becomes smooth and easier. All subsequent steps of auditing are dependent on vouching. Usually frauds and errors can be detected by vouching.

In the words of **De Paula,** *"Vouching is the essence of auditing."* The success of failure of Auditing depends on vouching. Audit work is impossible without vouching. It is, therefore, no exaggeration to say that *"the vouching is the soul of auditing."*

The following points will make clear the importance of vouching:

(1) Reliable examination: In vouching, the entries in original books of accounts are verified to ensure that the transactionsaregenuine;they are authenticated and comply with normally accepted principles of accounting. If a transaction is not authenticated or is not properly recorded, then the final accounts would not show a true and fair view of the profit or loss and state of affairs of business. The entries in the books of original entries are the foundation on which the correctness of entire accounting record is based. Thus, vouching tests the very base of accounting process.

(2) Examination of original evidences: Checking of entries is done by examining the original evidence supporting such entries. Vouchers are thus links between transactions and entries. By vouching the particulars of transactions, such as dates, amounts, the names of parties, etc. are known. Thus details are compared with the final evidence establishing the correctness of entries in books of accounts.

(3) Detection of errors at initialstage: By checking the entries, with original evidence, the errors and frauds can be located at an early stage. The maxim that 'the prevention is better than cure' is achieved as the vouching prevents the errors before they assume serious proportion.

(4) Keeps the auditor alert: Since the starting point of audit is vouching, the auditor can detect errors and frauds in the beginning of audit. If he finds any errors, he becomes more alert and careful and extends his checking to very important transaction. He resorts to auditing in depth' and can thus carry out his work in a more responsible manner. In case of *Armitage Vs. Brewer and Knott, 1982,* it was held that audit is dependent on vouching and if the auditor shows carelessness in vouching, he will be held liable for it.

1.5 POINTS OF BE CONSIDERED IN VOUCHING

While vouching, an auditor should keep in mind the following points :

(1) Serial number: The auditor should see that the vouchers are consecutively numbered according to date and the order of transactions. If this is not done then the auditor's time would be unnecessarily wasted in finding out required vouchers.

(2) Date: The auditor should carefully check the dates on vouchers. The vouchers should relate only to the year for which the accounts are audited. Otherwise the vouchers of earlier year may be produced again and cash or goods might be misappropriated.

(3) Name: The vouchers should be in the name of client. The transactions recorded in the books of a client would be correct only if they are supported by bills, documents and other evidences in the name of that particular client. The name of the party from whom the voucher is received should be compared with the name of supplier in the books of accounts.

(4) Address: The voucher should be addressed to the client in whose books the transaction is recorded. If the voucher is in the personal name of director, partner, or manager, the same may not be relating to business itself.

(5) Amount: The amount shown in the voucher should tally with the amount recorded in the books of accounts. The amount in voucher should be indicated both in figures and in words, so that the alterations in figures can be avoided.

(6) Particulars: The auditor should carefully examine the particulars mentioned in the voucher. From the particulars given in the vouchers, auditor is able to ascertain whether the item is of a revenue or capital nature. This distinction is of great importance, since the capital income and expenditure are shown in the Balance Sheet whereas revenue income and expenditure are shown in Profit and Loss Account.

(7) Approval and Signature: Each voucher should be properly approved and authenticated. The person who authorizes payment or other transaction should put his signature in support of having approved the voucher. The auditor should have with him specimen signature of various officers, with schedule of their powers.

(8) Revenue stamp: For payments exceeding Rs. 5000/- the relative receipts should bear revenue stamp of Re. 1.00. However, where the items are purchased for cash and a cash-memo is obtained, there is no need to obtain stamped receipt.

(9) Continuous vouching: As far as possible the auditor should complete the vouching of a particular period of a book in single sitting. If the vouching is kept pending or incomplete, then there are chances of figures being altered and a fraud being committed after the vouching is over.

(10) Cancelling the voucher: Once the voucher is audited, the same should be cancelled so that it may not be produced again. Rubber stamp, Seal or Ticks of particular color is used to cancel the voucher.

(11) Period: The auditor should pay particular attention to the period to which the voucher relates. If the expenditure is for the period beyond the accounting year of client, the proportionate amount of expenditure should be debited to prepaid expense accounts. Similarly, from verification of period, the auditor gets an idea about income received in advance, income due but not received for which correct adjusting entries should have been passed.

(12) Entry in the books of accounts: While examining vouchers, the auditor should see that correct entry is passed in the books of accounts and he should see that there is no voucher which is left to be recorded in the books of accounts. Moreover, as per details of voucher, correct classification of revenue and capital is done.

(13) List of Missing Vouchers: After vouching is over, the auditor should go through the relevant books or register and find out the un-ticked items. The items may not be ticked for want of vouchers. The auditor should prepare a list of missing vouchers and ask the person concerned to obtain the same. If he does not get the vouchers within reasonable time or if he has not offered satisfactory explanation about missing vouchers, he should mention the facts in his report. In several types of expenses vouchers are not received e.g. Tea and breakfast, cartage, etc. In such cases he should verify the signature of employees through whom the payment is made and should also see that the payments are approved by responsible person.

1.7 Verification & Valuation

The auditor has to give a certificate on the accounts examined by him that the Profit and Loss Accountant shows as a true and fair view of the profit or loss of business and the Balance Sheet shows a true and fair view of the state of affairs of the business. Hence it becomes the duty of the auditor not only to vouch the expenses and incomes, but also to verify and check the valuation of the assets and liabilities of business. He has to satisfy himself that the assets and liabilities do in fact exist, and they are properly valued.

1.7.1 MEANING OF VERIFICATION

Verification means verifying the truth of the existence, values and ownership of the assets. Before signing his report, auditor has to satisfy himself that the assets shown in the balance sheet really exist, they are in the name of his clients and the values shown are proper. The process of satisfying himself regarding all these points is ‘verification’.

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*."

According to **Joseph Lancaster** *"Verification of assets is a process by which the auditor substantiates the accuracy of the right-hand side of the Balance Sheet, and must be considered as having three distinct objects : (a) the verification of the existence of assets (b) the valuation of assets and (c) the authority of their acquisition"*.

From the definitions it can be inferred that verification involves the following:

(1) That assets actually exist.
(2) That the assets are acquired for the business.
(3) That the assets are properly valued.
(4) Whether the assets are clean or there is a charge on the assets.
(5) That its balance tallies with that shown in the balance sheet and is clearly and correctly shown in the balance sheet.

1.7.2 OBJECTS OF VERIFICATION

Verification of assets and liabilities is undertaken with the following objects:

(1) To satisfy himself about the existence of the assets.
(2) To see that assets and liabilities are valued on the basis of generally accepted principles and that valuation is consistent with that of previous year.
(3) To verify that the assets and liabilities not connected with business are not shown in the balance sheet.
(4) To verify that business assets and liabilities are included in the balance sheet and no item is left out.
(5) To see that the balance sheet shows a true and fair view of state of affairs of business.
(6) To see that the ownership and possession of assets are with the company.
(7) To check that no fraud or irregularity are committed in connection with any asset or liability.
(8) To see that the accounts of assets and liabilities are arithmetically correctly recorded.
(9) To verify that the all assets and liabilities are properly shown in the balance sheet according to rules and legal requirements of the institution.

1.7.3 DIFFERENCE BETWEEN VOUCHING AND VERIFICATION

It has been stated earlier that both vouching and verification are very important aspects to auditing. However, verification is a much wider term than vouching. The points of difference between the two may be stated as follows:

(1) Vouching means substantiating an entry in the books of account with the supporting vouchers like receipts, invoices, correspondence, contracts etc.

Verification means examining with regard to the assets shown in the balance sheet that they exist, are in the name of the company, are properly valued and are free from any charge.

(2) The object of vouching is to check that the entries made in the books of accounts are correct. Whereas the object of verification is to check the existence, valuation, ownership and possession of the assets.
(3) Vouching is carried out with the help of vouchers. Verification includes in addition to vouching, the checking of physical existence, valuation and ownership of the assets.
(4) Vouching is done at any time during the year. Verification is done only after accounts are completed and balances are drawn. .
(5) Vouching of assets is undertaken once during the life time of the asset. Verification of assets shown in the balance sheet is done every year.

(6) Vouching does not include valuation of assets and liabilities. Verification includes valuation of assets and liabilities.
(7) Vouching is the first step taken before verification. It involves examining the transactions when they take place. Verification is the next step after vouching is completed. It includes checking many aspects of assets and liabilities.

1.8 MEANING OF VALUATION

As we have seen earlier, an auditor is required to certify that the balance sheet shows, true and fair view of company's affairs. Naturally, if the assets and liabilities are shown at their proper values, the balance sheet would be true and fair. Hence the auditor has to satisfy himself that the assets are shown in the balance sheet at their true and fair values.

Now the problem is what the correct value of an asset is. The assets would be deemed to be properly valued, if valuation is made according to the generally accepted principles of accounting. For example, the fixed assets are to be shown at cost less depreciation to date. If this practice is not followed and if depreciation is more or less than the fair amount, the profit will be understated or overstated. A number of complications will then arise and the balance sheet will not show true and fair financial position of business.

Now what are the duties of the auditor with regard to valuation of assets? As stated above, he has to ensure that generally accepted principles of accounting have been followed. He is not a technical man and cannot ascertain correct values of all types of assets. Hence, he has many times to rely on the certificates of the trusted officials of the company. But he should exercise reasonable care and skill in satisfying himself that the values of assets are correct.

1.9 DIFFERENCE BETWEEN VALUATION AND VERIFICATION

1. 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

2. 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.

3. 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.

4. 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.

5. Vouching Verification includes vouching. Valuation does not include vouching.

6. 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.