# Diploma in Financial Management & Accountability

*- A joint initiative of TISS & FMSF*

## Course Material

## Audit

## Paper - VII

## Module - IV

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# UNIT- 7
# VERIFICATION OF ASSETS & LIABILITIES

## 7.1. VERIFICATION OF ASSETS

**7.1.1. Introduction**: Verification of assets is an important audit process. By convention its scope has been limited to inspection of assets, where it is practicable, and collection of information about them on an examination of documentary and other evidence so as to confirm:

- That the assets were in existence on the date of Balance Sheet;
- That the assets have been acquired for the purpose of the business and under a proper authority;
- That the right of ownership of the assets vested in or belonged to the undertaking;
- That they were free from any lien or charge not, disclosed in the Balance Sheet;
- That they have been correctly valued having regard to their physical condition; and
- That their values are correctly disclosed in the Balance Sheet.

**7.1.2. Audit for Bank balances:** The following steps may be followed in this regard:

- The Auditor should ask for direct confirmation from the bank. If the account balances are available on the internet, the Auditor should verify the balances from the bank's website. This will save the time taken by the bank to confirm the balances and it has a greater degree of authenticity as well.

- Bank reconciliation statement should be prepared and checked

- Long outstanding un-reconciled items should be verified and inquired further

- Inter-bank transactions, inter-project transactions should be carefully scrutinised.

- In case of a charitable organisation having FCRA registration, the Auditor has to be careful about the inter-bank transaction between the FCRA bank account and the local bank accounts. Because as per FCRA laws, separate books of account are required to be made for foreign source earning.

- Under no circumstances foreign funds should be mingled with domestic funds.

- Bank receipt and bank balances have to be related with various donor agreements and minutes of board meetings to determine whether there are any restrictions on the use of such balances.

- The bank statement should be carefully scrutinised for direct credits or miscellaneous receipts in the bank account which are not properly substantiated or explained

- Apart from the above, it should also be seen that cash receipts are deposited into the bank preferably daily.

- The paying slips for cash deposits are prepared by the person other than the cashier and further deposits is made by other person than the person who prepares it.

### 7.1.3. Land & Building

a) To confirm the ownership of the free-hold property, examine the original title deeds and the conveyance deeds. These documents will state the purchase consideration. As regards to leasehold property, the lease deed should be inspected to verify the period of lease and other obligations attached to it.

b) Legal expenses and conveyance charges in connection with the purchase of property can be properly considered as part of the cost of acquisition and charged to the asset account.

c) The auditor should ensure that any changes in the building plans have been approved by the Funding agency.

d) Land and buildings should be shown in the balance sheet at the cost or as per approved valuation. The basis of valuation should be disclosed.

e) The depreciation on the building should be verified. In case of Projects Assets, where 100% depreciation has directly been claimed in the year of purchase, depreciation can still be provided by creation of a depreciation fund and the assets account on both sides of the balance sheet

f) The repair and maintenance cost of the building should be verified. It is necessary for the auditor to scrutinize closely the expenditure on repairs, so as to exclude expenditure that could legitimately be considered to have added either to the life or the usefulness of the building. Such expenditure should be capitalized by adding to the building account while the amount incurred on repairs is written off.

g) Property received in donation or as contribution in kind should be reflected at the value in accordance with the guidance note issued by The Institute of Chartered Accountants of India and accordingly the grant or donation account should be credited.

h) Satisfy that the building comply with all the statutory obligations like the protection against fire, and payment of municipal taxes. Also verify that they are adequately insured.

i) The auditor should review the minutes of the trustees/Board members or other authorizing committee for appropriate approval against major purchase, addition, disposal, etc.

**7.1.4. Other Assets**: Apart from the relevant point discussed above, the Auditor should look for the following with regard to fixed assets other than land and building :

- A location wise detail of all the assets should be prepared/obtained;

- The Auditor should see that proper registers are being maintained showing particulars of various assets;

- Wherever possible physical verification should be carried out;

- In case of vehicles, the list of vehicles and the registration number should be verified from the original documents;

- The Auditor should see that proper distinction is made within the NPO's own asset and the asset taken on lease or rent;

**7.1.5. Investment:** With regard to the investments and funds held by the organization, the auditor should try to look from the following aspects:

- To ensure that the investments are in existence and a valid title belong to the organization.

- The investments are on the basis of the prevailing laws of the country and in particular should be seen that 11(5) of the Income Tax Act, 1961 has been complied with.

- The valuation of investments is in accordance with the generally accepted principles and go on to represent true and fair view of the funds they represent.

- The income generated from the investment are properly accounted and allocated to various funds and projects to which they belong.

- The principles of fund accounting are followed to reflect various investments and funds independently and inter-fund transactions are also treated in proper perspective.

- The nature of the investment and their classification should be examined. The existence of the investments should be physically verified at least once a year.

- The auditor should check the schedule so obtained or prepared and trace the balance to previous year's working paper

- The auditor should also prepare the Statement of investments purchased or sold during the year. In this regard, it is important to look into the authorization of various sales and purchase transactions.

- Physically inspect the investments, securities\shares. Care should be taken that investments belonging to one project are not shown again in another project.

- If the investments are held in the name of Trustees, Board Members, etc. The auditor should inquire into the matter and look into the necessary and requisite documentary supporting in this regard.

- In case the investment is made in immovable properties, it should be ensured that encumbrance free title is in the name of the organization.

In this context, the auditor should be careful to see that short term Project Funds are not invested in properties.

- With regards to the cost of investments, the expenditures incurred on account of brokerage, transfer fee, stamp duty, etc., should be verified.

- The auditor should review donor agreements, minutes books of the Board meetings and try to segregate investments on the basis of various projects under which they are held because each project will have its own conditions and restrictions attached to investments. In this context, inter-projects transfers and their validity needs to be inquired.

**7.1.6. Loans & advances:** Examine the period for which the loans are outstanding and enquire into the reasons thereof. Where the loans are given against the security, examine the adequacy of the security. Examine the system of adjusting the advances against supplies from the same party should be adjusted at the end of the year. It should be seen that:

- Every ledger has been sanctioned by the competent authority and a separate entry has been made in each case; and

- The ledger is balanced at periodical intervals;

- Confirmations are obtained from the concerned employees/suppliers/ others at least at the end of the period.

**7.1.7. Imprest or permanent advance accounts:**In checking the accounts, it should be seen that:

- An acknowledgement is obtained from the staff concerned when he first received the amount;

- The advance is recovered at periodical intervals on submission of proper expenditure vouchers duly passed for payment by the competent authority;

- No unnecessary payments are made out of the advance; and

- The permanent advances are not multiplied unnecessarily and the amount of the permanent advance is kept as low as possible.

## 7.2. VERIFICATION OF LIABILITIES

**7.2.1. Introduction:** The auditor has to report whether the Balance Sheet shows a true and fair view of the state of affairs of the company and Profit and Loss Account shows a true and fair view of the profit or loss for the period under audit. If liabilities are not provided for in respect of expenses incurred or in respect of the income received in advance both the Balance Sheet and the Profit and Loss Account would not show true and fair picture. Hence, the auditor should see that the provision is made in respect of all the known liabilities. He should verify all liabilities in the Balance Sheet. Besides, he should have a certificate from the top management or a partner or proprietor that a provision has been made in respect of all the known liabilities. He should see that purchases are not suppressed. When the goods are received and either consumed or sold or taken into closing stock, the purchase of such goods must be recorded.

The auditor should verify that all the outstanding liabilities are recorded fully. Accrued expenses must be recorded. An understated liability has the effect of overstating the income and also the net worth. A liability should not be overstated also. All genuine liabilities must be provided for. An overstatement of liabilities may lead to fraudulent disbursements. In normal course of checking these can be uncovered.

**7.2.2. Corpus Fund:** The contributions/grants received towards corpus should be vouched with reference to the letters from the donor(s). The interest income should be checked with investment Register and physical investments in hand.

**7.2.3. Unspent balance of grant received / restricted Fund:** This is the unspent balance of the funded program out of the grant received. This should be checked with sanctioned letter / agreement with the donors letters, the financial report sent to the relevant funding agencies. It is to be ensured that this fund appears separately in the balance sheet and is not merged with the general fund of the organization. It should also be ensured that the funds are represented by identifiable assets.

**7.2.4. Ear-marked Funds:** This should be checked with the sanctioned letter from the donors, board resolution of NGO, rules and regulations of the schemes of the ear-marked funds. It should also be ensured that the funds are represented by identifiable assets.

**7.2.5. General Fund/Unrstricted Funds:** Check the composition of this fund to ensure it does not include the unspent balance of funding agencies or the earmarked funds. The increase/decrease of this fund should be checked with the unrestricted income and the un-funded expenses of the organization.

**SELF ASSESSMENT QUESTIONS**

i) **What do you mean by verification of assets and liabilities?**

**ii) How do you verify the following -**

- **Cash balance in hand**
- **Bank balance**
- **Stock in hand**
- **Advance against project work**
- **Fixed Assets**

**iii) How do you verify the following liabilities?**

- **Corpus Fund**
- **Unspent balance of Funding Agency**
- **Outstanding liabilities and expenses**

**iv) What external evidences would you use to verify the following assets and liabilities -**

- **Bank Balance**
- **Unspent balance of funding agency**
- **Outstanding liabilities for certain purchases.**