

Chapter 6

Vouching

6.1 INTRODUCTION

Vouching - Meaning	- Vouching means the act of examining vouchers i.e. documentary evidences in support of a transaction. - It is used to ensure that various transactions for the period are fairly and truly recorded in the books of accounts.
Factors to be considered while vouching	- Voucher is properly dated. - It is in client's name. - It is duly authorised. - Voucher is complete in all respects. - It clearly shows nature and amount of receipts and payments. - After examination, voucher should be stamped/initiated.

6.2 SCOPE OF CASH TRANSACTIONS

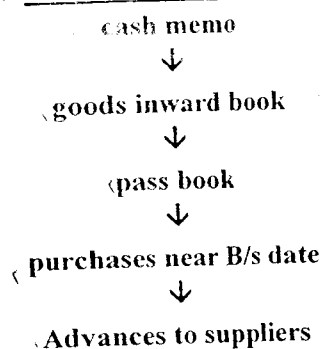
Considerations	(a) Review the I.C. system	- Auditor should thoroughly study I.C. system over cash transactions. - Carefully examine the authorisation levels. - Check whether any mechanical equipment is used like cash counting machines. - Ensure that I.C. system periodically reconcile the physical assets with their balances in books.
	(b) Ensure correctness of book keeping records	- Record of transactions should be checked in details. - Check whether entries have been made in books of account as per consistent accounting policy. - Thus, different errors can be detected.
	(c) Observance of Accounting principles	Special attention should be given to following: - Distinction between capital & revenue expenditure/receipts. - Accrual Basis of accounting. - Method of Depreciation. - Writing off of fictitious assets. - Adjustment of outstanding Assets & Liabilities.
	(d) Evidence of Transaction	- Auditor should check documentary evidence in support of transactions. - For eg; Payee's receipts, supplier's invoice etc. - Auditor should get as many external evidences as possible as these are more reliable than internal evidences.
	(e) Validity of Transactions	- He should check legal provisions, if any. - Refer to internal rules & regulations. - Check copy of contract, lease deed, agency contract etc.
	(f) Disclosure in final Accounts	- Auditor should check grouping of different items. - Eg: Directors remuneration should not be clubbed with employee's salary. - For this, he should see relevant legal requirements also.

Vouching is a process of checking accounting transaction with documentary evidence thereby

2. Casting or Totalling	▪ Totals of cash book and ledgers should be checked (in case where accounts are maintained manually) ▪ This is required to detect frauds done by over totalling/ under totalling. ▪ Special attention should be given to erased/altered figures.
3. Bank reconciliation statements	▪ BRS is prepared by client staff at periodical interval. ▪ Auditor should keep a record of it in his working paper file. ▪ Special attention should be given to year end transactions. ▪ Ensure about genuineness of items creating difference between cash book & bank book.

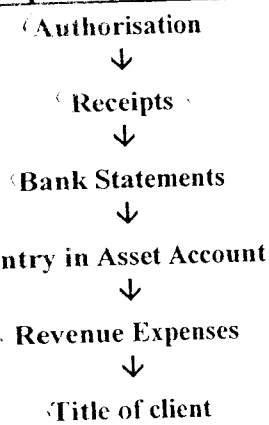
6.3 AUDIT OF PAYMENTS

1. Purchase of goods



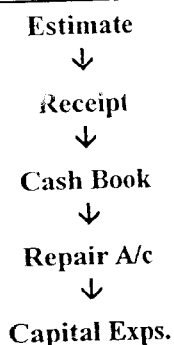
1. Check *cash memos* issued by suppliers.
2. *Goods inward book* should be checked.
3. If payments have been made through cheque, trace entry in bank statement.
4. Special attention is given to purchases made *near the balance sheet date* as goods might not been received.
5. Ensure that advances paid to supplier for future purchases have not been included in current year's purchases.

2. Payment for Acquisition of Assets



1. Examine whether payment is properly authorised.
2. Vouch receipt for the amount paid to the seller.
3. Trace the entry for payment in the bank statement.
4. Check capitalisation entry made in the books of account. Special attention to be given to "installation charges paid", to check whether same has been added to the cost of fixed assets.
5. Check that normal repairs etc. have been treated as revenue expenses & not debited to asset account.
6. In case of moveable property, check whether invoice has been made in client's name.
7. For immovable property, examine whether it is duly registered in client's name.

3. Repairs to Assets



1. Examine the payment for repairs with reference to estimate submitted by contractor.
2. Examine receipts issued by maintenance contractor, if any.
3. Trace relevant entry in cash book.
4. Check the entry in 'Repairs A/c' to ensure that all revenue expenditure in this connection have been properly accounted for.
5. Ensure that heavy repairs, which increases the life of asset have not been shown as repairs but treated as capital expenditure.

Installation
Expense
treated as
Capital exp

4. Traveling Expenses

Authorisation



Reasonableness



Bills



RBI's permission



Sundry expenses



To directors → Director's



Pass book



Entry in account



ARP

1. Ensure that all payments w.r.t. travel have been authorized/ sanctioned by proper official.
2. Check reasonableness of payments as per client's internal rules and regulations.
3. Vouch copies of the air/railways tickets and hotel bills.
4. Check whether permission of RBI has been obtained for expenditure in foreign currency.
5. Ensure reasonableness of sundry expenses such as daily allowance, conveyance and tips etc.
6. For travelling expenses claimed by directors, check whether these were incurred by them in the interest of the business.
7. Trace relevant entry in bank pass book.
8. Check posting in travelling expenses account.
9. Compare amount of travelling expenses with the previous year's figures and inquire into abnormal changes, if any.

5. Preliminary Expenses

Bills, agreement



Receipt



Resolution for reimbursement



Prospectus



Only preliminary exps.



AS 26

1. Various preliminary expenses relating to the formation of an entity such as registration fees, cost of printing of documents, legal fees etc., should be checked with reference to bills and agreements.
2. Check receipt issued by lawyer, accountant and printing house.
3. Examine resolution of BOD and the power in AOA, in case such expenses incurred by the promoters have been reimbursed to them.
4. Cross check the amount of preliminary expenses with that disclosed in the prospectus.
5. Check that no expense other than those constituting preliminary expenses are included under this head e.g. brokerage, underwriting commission.
6. Auditor should examine compliance with AS 26, with respect to accounting treatment of preliminary expenses.

6. Wages And Salaries

Internal control



Employee data



Arithmetical accuracy



Acknowledgements



Deductions



Retired employee



Dummy workman

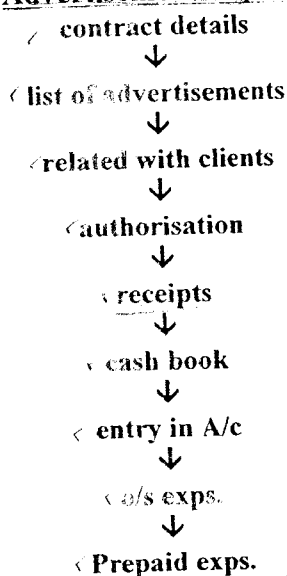


Bank statement

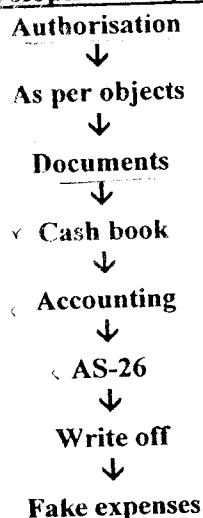


Unclaimed wages

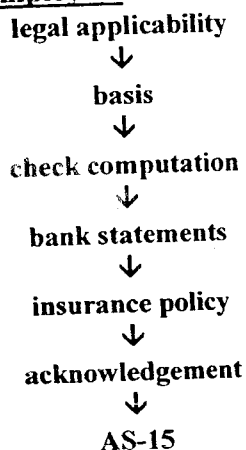
1. Examine internal controls relating to wages and salaries specifically on following areas:
 - Attendance record of employees
 - Appointment, promotion and transfer of employees
 - Disbursement of salaries and wages
 - Custody of wage records
 - Authorisation for disbursement of overtime
 - Payment of advance to staff
 - Control over dummy workmen
2. Examine the employee data such as name, wage rate, attendance record, etc.
3. Check the arithmetical accuracy of the payroll function.
4. Examine the acknowledgements by employees.
5. Check deductions w.r.t. TDS and Provident fund etc.
6. Ensure that employees who have retired or otherwise left the services of the enterprise, have not been included in the payroll.
7. Ensure that no dummy workman has been paid wages.
8. Check relevant entry in bank statement.
9. Pay special attention to unclaimed wages.

7. Advertisement Expenses

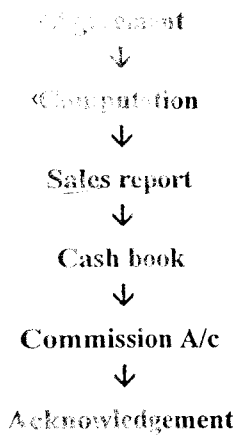
1. check contract with advertising agency.
2. Obtain complete list of advertisements, media wise i.e. newspaper, T V etc
3. Check that these relate to client's business only.
4. Examine authorisation of payment made.
5. Check receipt for amount paid.
6. Trace entry in the cash/bank book.
7. Check relevant posting in relevant account.
8. Examine that outstanding advertisement expenses have been shown as liability.
9. Check that advances paid w.r.t. same are shown as assets.

8. Research and development expenses

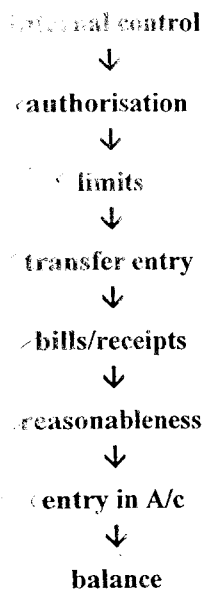
1. Examine authorisation for research & development expenses.
2. Check whether these are expensed as per objects of entity's business.
3. Examine relevant documents such as expenditure on material can be vouched by examining suppliers acknowledgement.
4. Trace entry in cash book / bank statement.
5. Ensure its proper accounting and disclosure in books of accounts.
6. Ensure compliance with AS-26.
7. Ensure that routine research cost has been written off to P&L account.
8. Check that no fake expense has been debited to research & development expenses account.

9. Retirement gratuity to employees

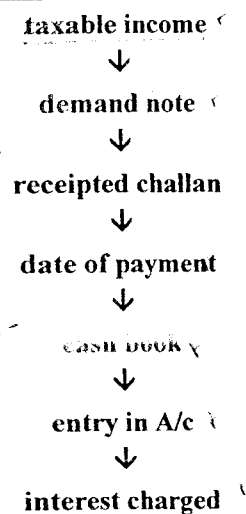
1. Examine the relevant legal applicability or any contract entered into between employer & employee to check requirement to pay gratuity.
2. Ensure that basis of computation of gratuity is valid and as per prevailing laws, if any.
3. Check computation of gratuity with reference to number of years of service rendered by retiring employees.
4. Trace the relevant payment entry in bank statement.
5. If any insurance policy has been taken to fund gratuity liability, ensure that premium deposited has been taken to P&L Account.
6. Check acknowledgement from employee who got gratuity in relevant financial year.
7. Ensure compliance with AS-15

10. Check on Commission

1. Check the agreement entered into with the agents.
2. Ensure that sales and commission computation has been made as per the agreement and commission is paid only to authorised agents.
3. Examine sales report sent by the agent during relevant year.
4. Trace the entry in cash book / bank statement.
5. Trace the entry in commission account.
6. Obtain acknowledgement from agents.

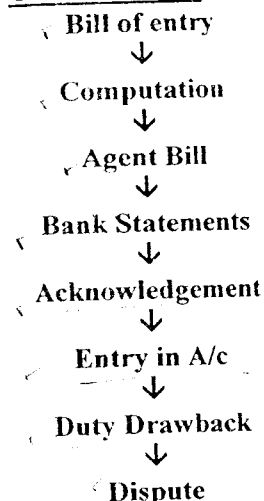
11. Petty cash expenses

1. Check the internal control over this area, as chances of misappropriation of cash are high.
2. Check authorisation level of persons having custody and control over petty cash.
3. Check the limit of imprest with a particular employee.
4. Trace the transfer entry from cash book to petty cash book to ascertain amount given to petty cashier.
5. Check the relevant voucher, bills, receipts in support of the expenditure.
6. Examine whether the expenditure have been duly approved by the authorised person. Check its reasonableness.
7. Trace entry into nominal account.
8. Examine balance of petty cash in hand.

12. Payment of income tax

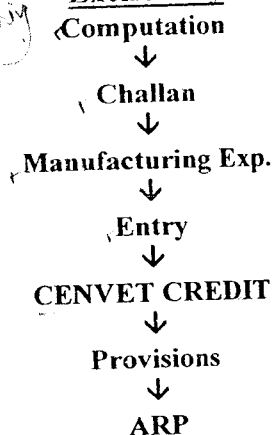
1. Ascertain the computation of taxable income as per provisions of the Income Tax Act, for eg. Computation of depreciation as per Income Tax Act.
2. Check Assessment order or demand notice issued by the tax authorities.
3. Examine receipted challan to check that amount shown therein is the same as shown in books of account.
4. Reconcile the due dates and actual dates of payment. Enquire any delay in actual payment (as per provisions of CARO).
5. Trace the relevant entries made in cash book.
6. Trace entries in income tax paid account.
7. Check whether penal interest charged on delayed payment of income tax has been shown as expenses in P&L account.

Import duty

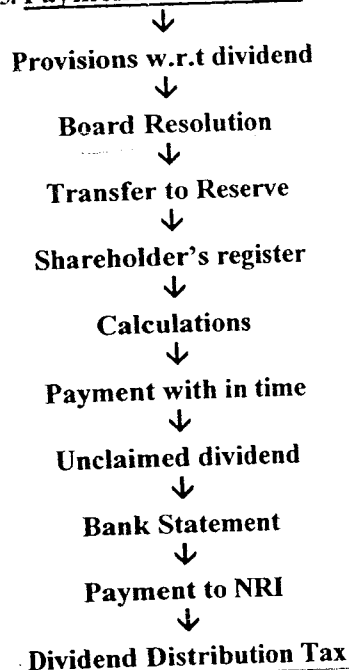
13. Custom duties

1. Examine "Bill of entry" to ensure that goods have been, in fact imported during the year.
2. Check whether calculation of customs duty has been made as per the applicable rate in force.
3. In case duty is paid through some clearing agent, examine agent bill.
4. Trace payment in cash book/bank statement.
5. Check acknowledgement from custom authorities.
6. Trace entry in custom duty paid account.
7. Verify claim for *duty drawback* by checking acknowledgement from authority.
8. In case of dispute regarding duty payable, check whether provision is properly made for the same.

Manufacturing

Excise duty

1. **Meaning :** Excise duty is levied on manufacturing, it becomes payable on release of excisable goods from godown/factory of the manufacturer.
2. Check the computation of duty paid to ensure that rate applied is as per prevailing rates.
3. Check payment w.r.t. duty by examining challans.
4. As it is levied on manufacturing, it is a manufacturing expense. Ensure about correct accounting treatment.
5. Trace the relevant entry in the nominal account.
6. Ensure that CENVAT credit has been correctly adjusted in the accounts.
7. For excisable goods manufactured, which haven't been released till B/S date, check whether provision for unpaid excise duty has been made.
8. Compare excise duty paid in current year with that of preceding year.

15. Payment of Dividend

1. Study the special provisions in MOA and AOA w.r.t payment of dividend, if any.
2. Examine Board resolution regarding rate of dividend.
3. Ensure that provision of the Companies (Transfer of Profit to Reserve) Rules 1975 have been adhered to.
4. Study the Shareholder's Register to ensure that payment is made to all registered shareholder.
5. Calculation of dividend should be checked.
6. Check that dividend has been paid within the time limit prescribed under The Companies Act.
7. Examine instances of unclaimed dividend.
8. Trace relevant entries in bank statement.
9. For payment of dividend to non-resident shareholders, ensure that RBI's permission has been obtained.
10. Check whether Dividend Distribution Tax has been paid.

16. Transaction with

A Ltd.

Board Resolution**Approval of CG****Disclosure of Interest****Approval of Interest of Price**

1. Board resolution is needed if,

- A director, or
- His relative, or
- A firm in which director/relative is a partner, or
- Private company of which director is a member,

Enter into contract with the company in question. Auditor should check whether resolution has been passed.

2. Moreover, if company concerned has paid up capital of Rs. 1 crore or more, even prior approval of CG is needed in addition to Board Resolution

3. Every director, who is interested,

- Directly or indirectly
- In contract with the company

Then, he must disclose his interest at board meeting

4. As per CARO, Auditor should check reasonableness of prices also.

17. Remuneration paid to directors

(1) For public company, certain requirements of the companies act have to be seen which are as follows;

(I) Specific provisions are required for remuneration as per

- Articles or
- Resolution in GM

(II) It can be paid as

- Fee for attending meetings
- Monthly/quarterly or annual salary for whole time director

(III) For director other than whole time director, approval of CG is required.

(2) Thus, Auditor should check the authorisation level to release the payment.

(3) Auditor should seek the attendance record from the company.

(4) Check the computation of director remuneration to ensure compliance with requirement of The Companies Act (sec 309 & 198)

(5) Ensure that proper disclosure has been made in financial statements w.r.t same.

**18. Payment controlled by
the Companies act'
1956**

Provisions of Companies Act are as follows which should be considered by Auditor:

1. Under sec 227(1A)(e) personal expenses charged to revenue should be reported by auditors.
2. Under section 293, BOD of a public company require consent of shareholder in GM for following:

- **Selling, leasing or disposing**

- Whole / substantially whole of
- Undertaking of the company

- **Remitting/giving** time for re-payment of any debt due by a director

- **Investing** compensation receive by way of compulsory acquisition of any

- Undertaking or
- Premises or properties of the undertaking

- **Borrowing** of money if

- money already borrowed together with moneys proposed to be borrowed

- will exceed aggregated of paid up capital & free reserves

- **Contributing** to

- Charitable fund or
- Any other fund (not related to business of company /to welfare of its employees),
- amount which exceeds ,
- Rs.50,000 or 5% of average net profit during 3 immediately preceding financial year (whichever is greater)

3. Under section 293A.

- A government company or
- a company which is in existence for less than 3 financial years
- Cannot contribute to any *political purpose*
- amount exceeding 5% of average net profits during 3 immediately preceding financial years

4. However as per section 293B, Board can make contribution to national defence fund without any restriction.

6.4 AUDIT OF RECEIPTS

1. Sales Internal control ↓ Authorisation ↓ Bills ↓ Cash sales summary book ↓ Cash memos ↓ Cash book ↓ Bank statement ↓ AS-9 Revenue Recognition	1. Examine the internal control over receipts from sales. Examine authorisation level for making cash sales & receiving amount there from. 2. Test check the few bills for ascertaining accuracy of rate, amount, discount & Sales Tax/ VAT etc. 3. In case a large number of cash sales are affected, check cash sales summary book maintained by the client. <i>Carbon copy of bills</i> 4. Examine copies of cash memos. <i>Issue 4</i> 5. Trace the relevant entry in cash book with reference to date on cash memos. 6. In case, daily cash collection are banked on next day, trace the same in bank statement on subsequent day. 7. Ensure that revenue has been recognised as per requirements of AS-9 "Revenue Recognition". 8. Cash sales during the year should be recognised even if physical movement of stock has not taken place. This point is specially to be considered with respect to sales near the balance sheet date.
<i>Handwritten: 11/06/16, Provide</i> 2. Sale proceeds of junk materials Internal control ↓ Records ↓ Production records ↓ ARP ↓ Rate ↓ Cash book ↓ Accounting treatment	1. Evaluate the internal control over generation, storage & disposal of junk material. 2. Check the records for sale & disposal of junk materials. 3. Check the production records to determine quantity of junk material. 4. Compare units of junk materials in current year with that of preceding few years. 5. Check the rate at which different junk materials have been sold. 6. Examine corresponding entry in cash book. 7. Examine whether it has been shown as sales or reduced from cost of product.
<i>Handwritten: Rent as per terms</i> 3. Rent Received Terms ↓ Records ↓ Calculation ↓ Receipt ↓ Confirmation ↓ Accrued rent ↓ Disputed ↓ Cash book ↓ Entry in A/c	1. Study various terms & conditions of agreements entered into with tenants. 2. Examine records of properties let out. 3. Ensure that calculation of rent has been made as per terms. 4. Check copy of receipts issued to tenant. 5. Obtain confirmation from tenants regarding amount paid by them. 6. For rent accrued but not received, check proper ness of accounting treatment. 7. If any outstanding rent is under dispute, examine whether provision needs to be made. 8. Trace relevant entry in cash book. 9. Check correctness of accounting treatment in nominal account. 10. Ensure that TDS been properly adjustment.

4. <u>Royalty Received</u> <u>Terms</u> ↓ Periodical statement ↓ Computation ↓ Acknowledgement ↓ Cash book ↓ Entry in account ↓ Accrued royalty	1. Study the terms of contract between client (author) & the publisher. 2. Check periodical statements received from publishers regarding number of books sold. 3. Check computation of royalty to ensure that it is as per terms. 4. Examine acknowledgement issued to the publishers. 5. Trace entry in cash book. 6. Ensure correctness of posting in nominal account. 7. Check adjustment regarding royalty due but not received.
5. <u>Commission received</u> <u>Terms</u> ↓ Computation ↓ Periodical statement ↓ Receipt ↓ Entry in a/c ↓ AS-9 ↓ Advance	1. Study the terms of contract with principal. 2. Check computation of commission. 3. Usually agent (Client) provides periodical sales statement to principal, based on which commission is calculated. Examine the statement as well. 4. Examine copy of receipts issued. 5. Trace entry in cash book & relevant account. 6. Ensure compliance with AS-9 "revenue recognition". 7. Check adjustment w.r.t advance received ensure that it has been shown as liability and not booked as income in the relevant year.
(6) <u>Income from investment /interest & dividend</u> <u>Schedule of Investment</u> ↓ Computation of Interest ↓ Dates ↓ Receipts issued ↓ Cashbook ↓ Entry ↓ Accrued income	1. Obtain schedule of investment & deposits made from the client and analyse it. 2. Test check computation w.r.t interest income. 3. Check due dates for interest & dividend & compare with actual date of receipt. 4. Check relevant entry in cash book with copy of receipt issued. 5. Ensure that full amount of interest /dividend has been taken to P&L account. 6. Ensure that accrued income in this respect has been accounted for as per AS 9.

Terms of agreement, Computation, Cash book, Accrued, Receipts issued

(7) <u>Sale of investment</u> Internal control ↓ Broker's note ↓ Computation ↓ Profit/loss ↓ AS-13 ↓ Entry <i>Cash/Bank A/c</i>	1. Review the internal controls over sale of investments. 2. Generally, investments are sold through stock broker, thus examine broker's note. 3. Test check the computation of amount received on sale as shown in broker's note as well as net amount received from broker (i.e. after deduction of brokerage and other charges) 4. Compute profit/loss as shown in P&L A/c by the client. 5. Ensure compliance with AS-13 "Accounting for Investment". 6. Trace relevant entry in cash book/bank statement.
(8) <u>Sale of assets</u> Internal control ↓ correspondence ↓ Copy of receipt ↓ Reasonableness of price ↓ Accounting ↓ Profit/loss on sale	1. Review the internal controls over this area including authorisation level for making the sale. 2. If asset has been sold through agent, examine correspondence with him. 3. Check the amount received with reference to copy of receipt issued. 4. Examine reasonableness of price by enquiring the management. 5. Ensure that sale proceeds have been fully accounted for. 6. Examine computation as regards profit/loss on sale and ensure that same has been properly accounted for.
(9) <u>Bad debts recovered</u> Bad debts ↓ Recovery ↓ Acknowledgement ↓ Bankruptcy dividend ↓ Cash book ↓ A/C treatment	1. Examine the bad debts appearing in client's accounts. <i>Previously</i> 2. Examine that all recoveries against this have been shown in books. 3. Examine acknowledgement issued to debtors. 4. In case receipt of bankruptcy dividends, check correspondence with official receiver. Note: when a debtor is sued for bankruptcy, entity has to prove to the official receiver that debt is due from him. Subsequently, amount is received generally in parts, which is known as bankruptcy dividend. 5. Trace relevant entry in cash book. 6. Ensure proper treatment in Profit and loss account as income. <i>and not to Dr A/c</i>

6.5 AUDIT OF SALES

1. <u>Internal controls</u> ↓ <u>authorisation</u> ↓ <u>nature of goods</u> ↓ <u>sales invoice</u> ↓ <u>cut off procedure</u> ↓ <u>source documents</u> ↓ <u>posting</u> ↓ <u>special discount</u> ↓ <u>confirmation</u>	1. Auditor should examine the internal control system in this area. 2. Examine whether sales has been authorised by a responsible official. 3. Ensure that goods are those which are normally dealt in by client. 4. Auditor should examine copies of sales invoices. 5. Ensure that each item of sales actually relates to the year concerned i.e. examine cut off procedures. 6. Examine the source documents (sales orders, sales invoices) generated with in the organization 7. Examine entry in sales account as well as in customer's account to ensure their correct posting. 8. Authority for granting special discounts should be examined. 9. Confirmation from the customers should be obtained.
2. <u>Goods on 'Sale or Return Basis'</u> <u>Option with buyer</u> ↓ <u>Requires approval</u> ↓ <u>Memorandum day book</u> ↓ <u>Entry in accounts</u> ↓ <u>Provision</u> ↓ <u>status</u> ↓ <u>included in closing stock</u>	1. It means that customer (buyer) has the option either to accept the goods or to return them with in a specified period of time. 2. Thus, it pertains to sales pending approval from customer. 3. The auditor should check Memorandum day Book. 4. Examine whether on the receipt of acceptance from the customer, proper entries have been made in sales book and customer's account. 5. The auditor should check that a provision for sales returns has been made against all the transactions for which the customer has the option to return the goods as on balance sheet date. 6. Check the status of goods sent on approval. 7. All such goods should be included in closing stock. However, these should be shown as sales if :— ▪ Goods have been formally accepted by customers; or ▪ The time period for returning the goods has expired or where no time limit has been fixed, a reasonable time period has elapsed.

**(3) Goods on
Consignment Basis**

Performa invoices
↓
Account Sales
↓
Sale price
↓
Difference between
cost & invoice price
↓
Commission
↓
Payment of commission
↓
Reconciliation
↓
No profit on stock in
hand

NOTE: It refers to goods that are sent by the principal to his agent, to be sold at principal's risk.

The person who consigns the goods is called consignor and the one to whom the goods are consigned is called consignee.

1. Entries in the consignment sale book should be checked with copies of Performa invoices sent to consignee.
2. Check whether all periodical statements i.e. 'Account Sales' have been received from each consignee.
3. The account sales should be verified to check sale price of goods sold and expenses incurred by the consignee.
4. Ensure that the difference between the cost & invoice price has been properly adjusted in accounts.
5. Check whether commission due to consignee is as per the consignment agreements.
6. Verify the payment of commissions.
7. Examine the quantitative reconciliation between the goods sent, goods sold and goods in stock with each consignee.
8. Ensure that no profit is booked on goods remaining in the hands of consignee at the year end.

**(4) Packages and
Empties**

Returnable
↓
Memorandum system
↓
Stock with customer
↓
provision for loss

1. Sometimes, the container in which a product is supplied to the customer is returnable to the seller.
2. Memoranda system should be adopted if customers pay for the containers and returns them within a stipulated time as per agreement. At the time of issue, customer's account is debited with the cost of containers and credited when they are returned. Such returned containers should be valued at cost or NRV, whichever is lower.
3. Containers for which period specified for returning them has not expired, should be treated as stock with the customer and are carried forward to next accounting year at depreciated value along with stock in hand of containers.
4. The auditor should see that a provision has been made for containers not returned by customers within time.

(5) Sales returns

Sales return book
↓
Credit notes
↓
Inventory records
↓
Other documents
↓
Entry in accounts

1. Examine sales return book with reference to copies of credit notes issued to customers and inward return notes.
2. Ensure that credit notes are properly numbered. Missing credit note numbers should be duly enquired in to.
3. Ensure that returned goods are sent to stores immediately. All inward return notes should be entered in inventory records.
4. The auditor should also examine other records such as Return inward register and Stores records.
5. Examine corresponding entry for return of goods in customer's account

Credit note sent for sales return

Debit to Sales
To Cost

Sales return
To Stores

Sales return
To Cost

Credit to
To Note - A note

Note

6.6 AUDIT OF PURCHASES

1. Purchases Internal controls ↓ authorisation ↓ Purchase invoice ↓ Relates to year ↓ Only w.r.t. goods ↓ Not for personal use ↓ posting ↓ external confirmation	1. Auditor should examine the internal control system in this area. Also examine whether these have been adequately authorised. 2. Examine related purchase invoice & purchase orders. Also check whether an invoice has been sent to the client at his normal business address. 3. It should be checked that it falls within the period under audit. 4. Ensure that purchases of capital assets are recorded in journal and not in purchase book. 5. Castings and carry forwards in purchase book and postings to ledgers should be carefully checked. 6. Ensure that Goods purchased are meant for the purpose of client and not for personal use of directors or officers. 7. Examine entry in sales account as well as in customer's account to ensure their correct posting. 8. Confirmation from supplier should be obtained.
2. Purchase returns Purchase return book ↓ Debit notes sent or credit note ↓ Inventory records ↓ Entry in accounts	1. Examine purchase return book with reference to copies of debit notes issued to suppliers. 2. Ensure that a debit note has been sent to the supplier or credit note from the supplier has been received. 3. Quantity returned as per the return note must be checked with storekeeper's record and return outward register. 4. Examine corresponding entry for purchase return in supplier's account.

6.7 POSSIBLE REASONS WHEN THE RATE OF GROSS PROFIT ON SALES SHARPLY INCREASES / DECREASES IN COMPARISON TO THE PREVIOUS YEAR

(a) Factors which increase gross profit undervaluation of opening stock overvaluation of closing stock expenses not taken into A/c higher sales taken in A/c expenses incurred taken into A/c	1. Undervaluation of opening stock. 2. Overvaluation of closing stock. 3. Change in the basis of valuation of closing stock. E.g. where the opening stock was valued at cost or market rate whichever was lower, valuing the closing stock at the market price which is higher than cost. 4. Inclusion of goods received on a consignment basis, in the closing stock. 5. Treatment of goods sent out for sale on consignment basis as regular basis i.e. after adding profit margin. 6. Wrong allocation of expenses, e.g. freight inward may be wrongly taken to the profit and loss account. 7. No provision or under-provision in the expenses account included in the Trading Account.
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(b) Factors which decrease the gross profit

↳ Expenses not accounted for
 ↳ Depreciation
 ↳ Increase in G.P.
 ↳ False income included

1. Overvaluation of the opening stock.
2. Under valuation of closing stock.
3. Change in basis of valuation of closing stock. For example where the closing stock was valued at cost or market rate whichever was lower, valuing the opening stock at the market price which is higher than cost.
4. Amount of goods purchased in the previous year, which were physically received in this year, included in the purchases of current year.
5. Reversal of the fictitious sale entries recorded in the previous year to boost the profits.
6. Excessive provision made for wages and other direct expenses.
7. Failure to account for goods sold.
8. Failure to take credit for the amount of an insurance claim in respect of goods lost in transit or destroyed by the fire.

6.8 VOUCHING OF LEDGERS – Summary of procedures

1. Bought ledger

Purchase

1. Examine the internal control system in this area. *IC*
2. Trace the balances of creditors' account.
3. Obtain confirmation from creditors. *External Confirmation*
4. Examine various transactions of purchases and purchase returns. → *Credit note need*
5. Examine transfer entries among ledger to ensure their correctness.
6. Examine accounts, having debit balance as it may be due to advances given to suppliers.

2. Sales ledger

1. Examine the internal control system in this area. *IC*
2. Trace the balance of debtors' account. *Debtor A/c*
3. Obtain confirmation from debtors. *External Confirmation*
4. Examine various transactions of sales and sales returns. → *Credit note have been issued*
5. Assess the adequacy of bad debts provision.
6. Examine accounts having credit balance i.e. when advance has been received from customers.

3. General ledger

1. Examine whether balances from cash book and other subsidiary books have been transferred.
2. Examine all these books to ensure about their correctness.
3. Trace the balance of ledger accounts and examine their arithmetical accuracy.
4. Analyse the balance at the year-end.
5. Ensure compliance with recognised accounting principles.