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Does Your Plant Register Record the Past or Threaten your Future?

As well as providing evidence in the event of loss and giving the basis of an asset management system, most businesses use their plant register as the main tool by which they arrive at and record the written down value of their plant and equipment.

It is very rare to find a plant register that is completely accurate as maintenance of the register is often neglected and occasionally abused. Inaccuracies in this seemingly simple document, whether inadvertent or intentional, may shortly expose directors and auditors to legal censure. This is already happening in the US and should be a matter of increasing concern in the UK.

Enron Aftermath

The business collapses and corporate scandals that began with Enron in 2001 and WorldCom in 2002, awakened the world to potential lapses in ethics and to creative accounting practices on a world wide scale. These were perpetrated by businesses that had been previously considered blue chip, whose accounts had been approved by auditors believed to be beyond reproach. The US Congress rapidly sought to restore confidence in American businesses and business practice, closely followed by other legislative and regulatory bodies, culminating in the Sarbanes Oxley Act of 2002.

Sarbanes Oxley

Sarbanes Oxley is thought to be the most radical business legislation ever enacted in the US and amongst other things, requires companies to evaluate and disclose the effectiveness of their internal controls in respect of financial reporting. This will be effective at all levels throughout the business and will affect not only internal accounts teams, but also those with operational responsibilities. Independent auditors are then required to "attest" (agree or qualify) the disclosure.

In 2004 the Public Company Accounting Oversight Board was established to oversee and investigate the internal and external audits. The board also has other wide ranging powers to set and police auditing standards.

In broad terms Sarbanes Oxley currently applies only to US public companies, but by extension, this includes any foreign company whose shares are traded on US stock markets or whose securities are registered there. While many European businesses have already taken its requirements in their stride, others have found compliance to be involved and expensive.

European Implications

We understand that the European Commission has met both the US Securities and Exchange Commission and the Public Company Accounting Oversight Board, to seek to modify the effect of Sarbanes Oxley on European businesses registered or whose equity is traded in the US. Evidently the US will accept a regime that gives 'equivalence' to Sarbanes Oxley requirements in the European jurisdiction, although what this 'equivalence' might be is unclear.

How far the requirements of Sarbanes Oxley will be adopted within the EC remains to be seen, although changes to EU Directive 8 are already in view, including the role and position of statutory auditors. European listed companies are now considering how they would be able to sign off on their internal controls if more stringent requirements similar to those stipulated by Sarbanes Oxley were to be adopted across Europe.

Fraud -v- Incompetence

The stated value of the plant and machinery operated by a business has become an increasingly important component of balance sheets, particularly as fewer companies own the premises from which they operate.

It is therefore increasingly important to ensure that the plant register is properly maintained and does not contain any items that should not be capitalised. Unfortunately, this is seldom the case. In the course of GVA Grimley's plant valuation work, registers are invariably found to contain items that have been sold or scrapped. Often these assets have already been written off and therefore do not overstate the book value, but this is not always the case. Maintenance of an accurate plant register is a task which no-one enjoys and may be likened to cleaning the Augean Stables, in that years of neglect need to be rectified in a very short time and the problems continue to accumulate whilst others are removed!

More seriously, we have found a number of cases, (worryingly in the plant registers of Plcs) where items which should not be treated as plant, have been intentionally posted to the plant register and capitalised. In one Plc alone, these included:

- Repairs (to plant and buildings!)
- Engineers' travel and subsistence costs
- Consumables
- "Consultancy"
- Storage charges
- Security costs
- Equipment hire charges
- Transport charges
- Hire Purchase interest
- Lawyers' and Accountants' fees

Capitalising these items distorts the balance sheet, overstating the value of the plant and machinery and as they are excluded from the profit and loss account the profitability of the business is also overstated. The careless book keeper's classic "double whammy"!

Protection for the company and the auditor

The line between fraud and incompetence is often very fine indeed, but Sarbanes Oxley is only concerned with misrepresentation and cannot differentiate between negligence and deliberate falsification.

The company and the auditor can however be protected by the use of an independently prepared professional valuation, which will provide an accurate inventory and an independent value to be posted in the balance sheet. The inventory and the reported values can then be used as the base from which to structure the plant register and values in future years (but see the Augean Stables issues above!) or the valuers can be instructed to revisit the valuation annually, thus continuing to safeguard the company and the auditor.

There are added benefits

Whilst the valuation is being prepared, it can also be structured for a number of other purposes. Different bases of valuation can be applied to the inventory compiled for the valuation which will also:

- demonstrate precisely where the value in the plant and machinery is located
- enable unencumbered plant to be used as a basis on which an asset based loan can be based
- review the company's sums insured

As the impact of Sarbanes Oxley spreads to Europe, it can be assumed that companies will seek to reassure themselves that their financial statements reflect the financial health of their businesses and their auditors will wish to ensure that their reports similarly reflect the true picture. Commissioning a plant valuation will take one variable out of what will inevitably become a complex equation.

Get in early before the rush!



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