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## **Illustrative Bank Branch Audit Programme for the Year ended March 31, 2017**

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### **Introduction**

In present scenario of Audit of Branches of Banks, the most important aspect is proper planning. Planning means advance thinking and that should be done based on knowledge of branch business. It is important to have knowledge about Composition of Business of a particular branch which is under audit. Because of variety of products, auditor cannot apply the same yardstick for the branches under audit. Today, the whole process of banking is computerized however; the Audit Report is required to be signed manually after physical checking of records, documents and accounts maintained under CBS.

**The branch audit generally may be bifurcated in to following 3 categories.**

- a. Audit of Advances.
- b. Audit of all other items in the Trial Balance (TB).
- c. Ensuring various Compliances like Banks internal closing circular, RBI circular, LFAR, etc.

**Following are the generally followed steps for conducting of Branch audit;**

1. Appointment / engagement letter for Branch Statutory audit, with closing circulars.
2. NOC from the previous auditor
3. Pre-Audit discussion with branch
4. Audit planning
5. Execution of the audit as given in the **Annexure I**.
6. Discussion of the draft branch audit report with bank
7. Preparation of Memorandum of Changes and effect of the same in books of account of bank.

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8. Review of the Post Memorandum (Post MOC) trail balance and reconciliation with the pre memorandum (Pre MOC) trial balance to ensure the correct accounting effect of memorandum of changes.
9. Submission of audit report to branch and copy to central statutory auditors.

### **Following are the area wise documents to be collected and reviewed for conducting branch audit;**

1. Trial Balance as on 31<sup>st</sup> March
2. Closing circular issued by Bank's head office for conducting branch audit – Every bank issued the closing circular which contain the concern areas and list of certificates required to be certified by the branch auditor
3. Review of previous years auditor report / LFAR
4. Latest RBI master circular for “Income recognition and assets classification”
5. List of comments of RBI inspection report towards the branch
6. Latest branch concurrent audit report with their compliances
7. Copy of vigilance enquiry or any special investigation reports
8. Comparative analysis of the trial balance with the last year's audited trail balance. Review the major changes during the year.
9. Review of Ghosh and Jilani committee Recommendations.
10. Documents related to verification of advances –
  - List of stress advances (SME-2) as on 15<sup>th</sup> March (stress advances / SME-2 report indicate the list of advances which are overdue for more than 60 days and if the same is not regularized before year end i.e. 31<sup>st</sup> march than the advance will become NPA )
  - List of new sanction made during the year
  - List of account referred for Restructuring / CDR
  - List of Bank guarantee and Letter of credit
11. Documents related to NPA's
  - List of NPA accounts as on 31<sup>st</sup> March
  - List of accounts upgraded during the financial year
  - List of accounts downgraded during the year
  - List of early mortality cases for the year under audit
  - Details of the NPA classification with secured /unsecured details and NPA provision amount

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- Review of the valuation report of loan account. Valuation report older than 3 years cannot be consider as security (1 year in case of stock) and 100% provision need to provide on the expired secured portion.
12. Fixed Assets
- Fixed Assets register as on 31<sup>st</sup> March
  - List of new assets purchased during the year
  - List of fixed assets sold during the year
  - Physical verification report of branch fixed assets if conducted during the year
  - Depreciation working as on 31<sup>st</sup> March
13. Bank reconciliation
- List of bank account which branch maintained with other banks
  - Reconciliation statement of all banks account as on 31st march
14. Inter branch reconciliation
- Inter branch reconciliation statement
  - Provision for net outstanding debit balance for more than 6 month (refer RBI circular DBOD No. BP.BC. 73 /21.04.018/2002-03)
15. Cash
- Physical cash balance verification during branch audit period
  - Report of the physical cash verification conducted by branch on 31st March

### **Audit of Advances**

Audit of advances is discussed elsewhere in the journal under appropriate article. However from the angle of planning following aspects must be kept in mind:

1. **Obtain top exposure accounts:** It may be advisable for a branch auditor to ask the list accounts/ exposures along with all the details such as status, overdue amount and security etc. before starting of the audit.
2. **Obtain the list of stressed accounts:** The banks monitors stressed accounts on daily basis. The account that generally has overdue beyond 60 days or likely to slip to NPA at the quarter end is termed as stressed account (some banks may use different terminology). It is advisable to obtain such list of stressed accounts at least 15 days ahead of the closing date i.e. say stressed account list as on 15<sup>th</sup> March. This will provide the auditor a ready

list of such accounts. The auditor then can scrutinise each to know whether the account has slipped or if not whether has been kept standard by unusual transaction that cannot be termed as business transaction. Like deposit and withdrawal of cash, just to show the credit turnover during the quarter in cash credit account.

3. **Obtain the list of restructured accounts:** Restructured account portfolio requires separate additional provisioning. It is necessary to obtain the list of such accounts and ensure whether the restructure is as per the RBI directives. As per latest RBI guidelines, all new restructure / CDR account will be classified as NPA.
4. **Obtain the list of CDR accounts:** Generally CDR is not applicable to Cooperative banks. However in case the account is in consortium with any PSB/ Private bank, CDR may be applicable. In case such an account is found, ensure the compliance with the RBI guidelines in respect of CDR accounts. As per latest RBI guidelines, all new restructure / CDR account will be classified as NPA.
5. **Obtain the list of unsecured exposures above Rs. 25 Lacs.:** Unsecured exposure has significant impact on the bank, if slips to NPA. Many times such accounts are reviewed in the traditional manner. These require close monitoring not only from the perspective of financial parameters of the prudential guidelines but also non-financial parameters that give signals of the possible ill health. The banking industry has faced severe damages on account of non-identification of such non-financial parameters.
6. **Early mortality cases:** Any advance slippage to NPA within 12 months of its introduction is called early mortality case. Early mortality cases invoke penalty to the sanctioning authorities. This will have to be checked to understand the reason for such happening to avoid such cases in future and also to find out whether there are any cases classified as performing on some untenable ground to push it beyond early mortality.
7. **Upgraded accounts during the Year:** Review of the upgraded accounts is one of the important area to be check during audit. As per RBI circular, the account will get upgraded when arrears of interest and principal are paid by the borrower. After recovery, the accounts will get upgraded to standard assets. There should not be any overdue in borrower accounts as on date of up-gradation. The recovery in the accounts need to be review specially in

cash of cash credit accounts where the borrower rotate the fund just to keep the account as performing assets.

8. **Evergreening of accounts:** Evergreening refers to the practice of giving a fresh loan to repay an old one. Technically, evergreening refers to the practice of managing the balance sheet through means, which may not be violating banking laws in letter, but breaching them in spirit. To illustrate and to make it more clear : say a bank disburse a loan of Rs 10000 to a borrower and the account become overdue after a year or two , the same bank sanction a loan of Rs 20000 or Rs. 30000 which enable borrower to repay first loan. Therefore, the source of recovery needs to be review in case of stress accounts.
9. **Other routine checks:** The auditor may engage into other routine check of advances to satisfy himself such as classification of advances, new sanctions during the year, monitoring mechanism and provisioning under prudential norms. It may be pertinent to mention here two broad aspects that are heavily dependent on the branch auditor relating to advances. Also these are one of the most strong argument, amongst many, why branch audits are necessary even in CBS environment;
  - **Checking of documentation:** Documentations for newly sanctioned advances along with their enforceability, review documents and its appropriate reflection in CBS
  - **Security value for provisioning:** After classification, the most important aspect in presenting the true and fair view of the financial statements of a bank is correct provisioning amount. This highly depends on fair assessment of security value. The base documents relating to the valuation are usually available at the branches. Correct depiction thereof in the CBS is a crucial check.

### **Audit of other Items in Trial Balance**

It may not be necessary to elaborate on this point as this has been basic skill of auditing profession. However, following aspects may require specific attention of a branch auditor:

1. **Suspense, Inter Branch reconciliation and any other pending reconciliation item in TB:** As per the RBI guidelines, any debit entry in these accounts appearing for more than 6 months require 100% provision.

2. **Provisions other than relating to advances:** Year-end accounting provision that do not get generated through CBS require specific attention at the branch level.
3. It may be advisable to do a comparative study of last year end, half year and current year end figure comparison. This throws lot of insights into the branch operations.

### **Ensuring various compliances:**

Generally the branch requires following various compliances in respect of audit:

1. **Concurrent Audit report:** Any comments or remarks in the concurrent audit report that the branch is required to comply with.
2. **Compliance to RBI Inspection report:** If RBI has conducted inspection in the branch, the comments in the report need compliance. Any non-compliance under the pretext that the bank has represented to RBI to reconsider the observation should not be accepted. RBI has clearly taken a stand that unless auditor is physically shown a letter of reversal from RBI comments in their report must be adhered to.
3. **Compliance to Internal audit report:** If the bank has conducted internal audit, which usually an internal exercise, obtain the report and check for the compliances thereof.
4. **Stock audit report:** Generally an account having exposure of Rs. 5 Cr. and above requires stock audit, the compliance thereof should be commented upon. Also any adverse comment in the report needs to be dealt with appropriately.
5. **Application of interest in CBS:** Generally bankers always argue that the interest is calculated by the system and requires no cross verification. While this is true, the correct calculation by the system is subject to correct input by the branch staff relating to interest. Hence input of interest rates requires test check.

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**Annexure I**

<b>Details of the Authorised Persons of the bank</b>	<b>Branch Manager:</b>
<b>Others (Specify):</b>	

<b>Audit Aspects</b>	<b>Covered By Whom</b>	<b>Extent of Check</b>
<b>General</b>		
1. Engagement letter to the appointing authority		
2. Letter for NOC to previous auditors		
3. Meeting and discussion with the bank branch management and understanding the profile of the branch and its business and take a note on the same.		
4. Letter of requirement to the Branch		
5. Review of <ul style="list-style-type: none"> <li>• previous year's audit report/ LFAR,</li> <li>• current period's Internal Audit Report/ Concurrent Audit Report</li> <li>• Revenue Audit Report</li> <li>• RBI Inspection Report</li> <li>• compliance of the branch to all of the above and</li> <li>• any other special review report.</li> </ul>		
6. Physical verification of <ul style="list-style-type: none"> <li>• cash,</li> <li>• Gold (for Gold loan)</li> <li>• and valuable securities.</li> </ul>		
7. Note down <ul style="list-style-type: none"> <li>• Shortage of cash appearing in Trial Balance</li> <li>• Difference in physical verification of gold</li> </ul>		
8. Physical verification of Investments (obtain certificate from bank manager for the same). If investment is hold /done by the Branch		
9. Understand the system in CBS at Branch <ul style="list-style-type: none"> <li>a) verify controls</li> </ul>		

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Audit Aspects	Covered By Whom	Extent of Check
b) verify exceptional report c) understand the editable & uneditable fields at Branch, d) system of downgrading & upgrading of accounts, e) interest calculations, f) Generation of reports relating to advances classification and Capital Adequacy calculation, etc.		
10. Compliance of instructions issued by bank's year and closing circulars, other relevant internal instructions/circulars, Master circulars and other notifications issued by RBI, significant accounting policies of the bank Mandatory Accounting Standards/Auditing Standards and other notification.		
11. Prepare a list of various closing returns to be verified and certified, and then checking of the same during the audit.		
<b>Checking of Balance Sheet Items</b>		
<b>1. Checking of the advances:</b>		
<ul style="list-style-type: none"> <li>Take list of all advances along with facility wise limits, outstanding, Name of Lead bank, Credit Rating, Credit summations in the account, last date of submission of stock statement, date of review of account, etc. This shall help to select the accounts for scrutiny in detail.</li> </ul>		
<ul style="list-style-type: none"> <li>Critical review of all large advances and their reporting as per prescribed norms.</li> </ul>		
<ul style="list-style-type: none"> <li>Classification of advances as per IRAC norms.</li> </ul>		
<ul style="list-style-type: none"> <li>Latest valuation of security given against advances.</li> </ul>		
<ul style="list-style-type: none"> <li>Provisions on NPA as per IRAC norms.</li> </ul>		
<ul style="list-style-type: none"> <li>Review of all major restructured cases along with the compliance of</li> </ul>		

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<b>Audit Aspects</b>	<b>Covered By Whom</b>	<b>Extent of Check</b>
norms as per RBI Guidelines.		
<ul style="list-style-type: none"> <li>List of all SMA 2 accounts and reporting of the same to concerned authorities.</li> </ul>		
<b>Loan Accounts (Performing)</b>		
I. Review of all large advances with balance of lower of 5 % or Rs.2 crore of total advances.		
II. Review of loans sanctioned during the year.		
III. Review of other advances on test check basis.		
IV. Review of adverse comments by Concurrent auditors, RBI/internal inspectors and the reply given and corrective actions taken by the branch.		
V. Review of suit filed and decree accounts on sample basis with respect to provision thereon and progress of recovery thereof and Classification as per IRAC norms		
VI. Review of accounts upgraded during the year from NPA to standard. and ensure full recovery of total overdues before upgradation		
VII. Review of all accounts frequently exceeding limits/DP and watch-list accounts		
VIII. Also verify all the credit card dues which are overdue & debit balances in SB A/c		
IX. Check Drawing Power calculation in detail as per the norms of the bank.		
<b>Loan Accounts (Non Performing)</b>		
I. Review the accounts which are classified as NPA during the year w.r.t Security Value, Interest Reversed, Date of NPA, provisioning thereon etc.		
II. Review the annual stock audit report for the NPA with balance of Rs.5 cr. and above & latest valuation report for the immovable properties in case the		

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Audit Aspects	Covered By Whom	Extent of Check
valuation is older than 3 years.		
<b>NOTE:</b>		
(i) Following aspects of the advances to be verified:		
<b>Pre sanction:</b> System of credit Appraisal and review/renewal.		
<b>Post sanction:</b> Compliance of terms of sanction, documentation, end use of funds.		
<b>Monitoring:</b> Stock and Book statements, drawing power, insurance, inspection of stock/security, operations in the account, etc.		
(ii) All the accounts verified in category (i) to (x) should be documented.		
2. Verify controls in respect of the following important items of assets. (i) Dual custody of cash (ii) Custody and issue of /pay orders/other stationery items etc. (iii) ATM cash as per books and actual balance tallied at year end.		
<b>3. Fixed Assets</b>		
I. Checking of additions/deduction/transfers of fixed assets, supported by proper bills/invoices and confirmation of date put to use. Compliance of Accounting Standard related to fixed assets		
II. Checking of Depreciation on additions, deduction during the year and on existing assets as per the policy of the bank.		
III. Verification of Fixed Assets Schedule for furniture & fixtures and other assets and reconciliation with figures appearing in the Balance Sheet and FA management software used by the bank (if any).		
<b>4. Deposits</b>		
a) Verification of Anti Money Laundering guidelines and		

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<b>Audit Aspects</b>	<b>Covered By Whom</b>	<b>Extent of Check</b>
Compliance with KYC norms on test check basis		
b) that overdue deposits,		
c) Check TDS compliance on the interest paid and on test check basis checking of Form 15G & 15H and confirm whether those forms are submitted with respective Income Tax Authority		
d) Movement of Deposit vis-à-vis movement in interest expense.		
<b>5. Inter-Office &amp; Suspense A/c:</b>		
1. Reconciliation of accounts with other banks, head office and inter branch adjustment accounts.		
2. Inter Office Reconciliation (IOR) Accounts: I. Verify Inter Branch Items In Transit (IBIT) account for old entries. II. Compare on test Check basis, the balance and the entries in IOR Accounts with the copies of the statements submitted to the IOR department/s. III. Old un reconciled entries are being provided/ reported to HO for provision		
3. Detailed checking of suspense accounts – credit as well as debit schedules. i.e., Nominal ledger.		
<b>Balance Sheet Finalisation</b>		
1. Scrutiny of Balance Sheet, particularly –		
i) that all the balances are shown in proper heads and broadly compare previous year figure to understand material variance ii) Check for any negative balance in the trial balance (i.e. assets / expenses having credit balances and liability / income having debit balances)		

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Audit Aspects	Covered By Whom	Extent of Check
ii) check in case of advances that:		
a) interest accrued but not due on loans is not included in advances.		
b) credit balances in O/D, C/C inoperative current accounts should not be netted off with advances and the same should be shown under demand deposits.		
c) Verification of Anti Money Laundering guidelines and Compliance with KYC norms on test check basis		
2. Checking, (i) Liability under Bank Guarantee/ L/C and effects of expired BGs. (ii) Reconciliation of General Ledger and Subsidiary Ledger.		
<b>Checking of Profit and Loss Items</b>		
1. Test checking of interest on deposits, (particularly, Interest checking should be done on test basis for the period subsequent to the period of revenue/ concurrent audit). Ensure that interest provision on overdue F.D. has been made as per latest RBI guidelines. Check the system is properly configured to check the interest calculation and the changes in interest rate is changed in system on respective dates		
2. Test checking of interest/commission on various advances, bills, L.C., Guarantees, etc.		
3. Test checking of discount/commission on bills discounted and others income like commitment charges, processing fees, recovery of insurance/ legal fees etc.		
4. Derive various ratios of items of income with comparable and related assets (like Avg. Interest Income to Average Advances etc.) and verify major		

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<b>Audit Aspects</b>	<b>Covered By Whom</b>	<b>Extent of Check</b>
movements or variances.		
6. Checking of interest in NOSTRO Accounts debit balances.		
7. Verification of recovery on account of locker rent, staff accommodation, etc., with details of arrears, if any.		
8. Commission income on account of Government Business, i.e., collection as well as remittance of Income tax, sales tax, excise duty, etc.,		
9. Details of Prior Period items of Income as well as expenses and complete details of provisions to be made, if any.		
10. Booking of Interest Income on account of partial recovery in NPA's.		
11 Note down the reasons for material variances, if any		
<b>Others</b>		
1. Checking of statement of frauds adequacy of provision, timely reporting to competent authority, recovery and movement in balances.		
2. Checking of statement of claims against the bank not acknowledged as debt.		
3. Checking of Foreign Currency forward exchange contracts showing sales and purchase separately. Review of NRE and FCNR accounts, if any.		
4. Checking of Guarantees given on behalf of Constituents.		
5. Checking of Acceptance, endorsements and other obligations, i.e., L/C and bills accepted by the bank on behalf of customers.		
(Particularly check in case of Clause 4 and 5 above, whether the above guarantees and L/C issued are within the powers of the authorised person and proper procedures have been followed for issuing the same. Review the position of the above as at the year-end)		
6. Other contingent liability, if any.		
7. Checking of and preparation of Interest Subsidy certificate (as per various RBI & Government schemes), correct accounting & whether the same are		

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Audit Aspects	Covered By Whom	Extent of Check
given to the eligible .borrowers.		
8. Checking of write off proposal and DICGC claims, sharing of recovery, etc.		
9. Checking of annual returns on protested bills/ recalled debt accounts (PB/RD).		
10. Checking of LFAR schedules and preparation of LFAR. (Detailed planning for preparation of LFAR be done at the time of commencement of audit and detailed guidance be sought from the chapter on LFAR in this guidance note).		
11. Checking of Tax Audit annexures and preparation of Tax Audit Report.		
<b>Final Audit and Reporting</b>		
1. Preparation of Audit Report as per format prescribed under SA 700, ICAI and under any other regulatory authority.		
2. Preparation of memorandum of changes for changes to be made in classification of advances and in any item of asset/liability and profit and loss account with other remarks and/ or information which requires further attention at Regional/Zonal Office level.		
3. Preparation of Tax Audit Report.		
4. Preparation of Long Form Audit Report (by giving annexures where ever necessary)..		
<b>To collect the following Certificates:</b>		
1. Physical verification of the fixed assets carried out on March 31, 2017/During the year		
3. Physical verification of Investment carried out on March 31, 2017/ During the Year. If investment are held or appearing in the Trial Balance.		
3. Physical verification of the cash & other items as on March 31, 2017.		
4. Written Representation Letter.		
<b>To verify and issue the certificates (as applicable): Illustrative list</b>		
1. Certificate of Ghosh and Jilani		

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<b>Audit Aspects</b>	<b>Covered By Whom</b>	<b>Extent of Check</b>
committee Recommendations.		
2. Certificate giving details of claims lodged with DICGC / ECGC however, rejected by them		
3. Risk weighted assets as per the capital adequacy report (BASEL II & III).		
4. Certificate for treating an account as bad or doubtful of recovery as per the requirement of DI and CGC.		
5. Subsidy claim under Prime Minister Rojgar Yojna Or any other scheme of the Central/State Government.		
6. Certificate for Interest Subvention		

Prepared by:

Reviewed by: