

Statutory Audit of Bank Branches



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Western India Regional Council Of Institute of Chartered Accountants of India

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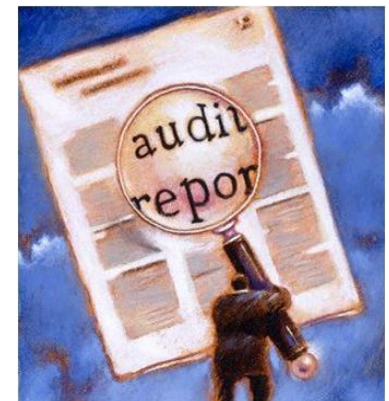




Today's Agenda

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- Reporting & Certification
 - LFAR
 - MOC
 - Audit Report
 - Tax Audit Report
 - Jilani & Ghosh Committee
 - Other areas/certifications





Introduction - LFAR

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- Long Form Audit Report 'LFAR'
- Introduced in 1985 – to PSB and then to all banks
- Revised in 1992-93 & 2003
- Submission of LFAR by CA – below cut off
- Detailed questionnaire formulated by RBI (SBA)
- Not a substitute for AR under SA 700
- Important tool to communicate with Management and Central Statutory Auditor



Main Objective

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- Reporting on internal controls, processes and systems followed in branches
- Provide useful information to assist the banks and the regulators with regard to matters/ issues that come to the notice of the auditors in the course of statutory audits of banks/ bank branches
- Questionnaire Form – Reply by Auditor
- Descriptive & may be supported with Annexures
- Supported by MRL





Broad Areas Covered

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- Assets
 - Cash & Bank
 - Money at call & short notice
 - Advances
 - Investments
 - Other assets
- Liabilities
 - Deposits
 - Other liabilities
- Contingent Liabilities



Broad Areas Covered

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- Profit & Loss
 - Revenue Recognition
 - Divergent trends
- Other General areas
 - Books, & records
 - Reconciliations of control accounts & subsidiary records
 - Inter branch accounts
 - Audit & Inspection
 - Fraud
 - Other Miscellaneous



Areas Covered (Specialized Branches)

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- Dealing in FOREX
- Dealing in very large advances
- Asset Recovery Branches
- Clearing house operations / service branches



Certain Crucial Clauses

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- Assets - Cash
 - cash balances in excess of fixed limits & its reporting
 - adequate insurance cover
 - effective joint custody
 - Checking at periodic intervals as per procedure prescribed by competent authority
- Balances with RBI/SBI & other banks
- Money at Call & Short notices
- Investments (Outside India & in India)



Certain Crucial Clauses

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- Assets - Advances
 - Large Advances
 - Credit Appraisal
 - Sanctioning/ Disbursement
 - Documentation
 - Review/Monitoring/Supervision
 - Guarantees and Letters of Credit
- Other Assets
 - Stationery and Stamps
 - Suspense Accounts/Sundry Assets



Certain Crucial Clauses

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- Liabilities - Deposits
 - Interest rate applied
 - Inoperative accounts
 - Window dressing
 - Matured and overdue deposits

- Other Liabilities
 - Sundry Deposits/Bills payables

- Contingent Liabilities



Certain Crucial Clauses

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- Profit & Loss
 - Interest rate applied
 - Income Recognition as per IRAC norm
 - System for adjustments for discrepancies
 - system of estimating and providing interest accrued on overdue/matured term deposits
 - divergent trends in major items of income and expenditure



Certain Crucial Clauses

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- General
 - Books & Records
 - Computerization
 - Under CBS or not & extent of computerization
 - System of hard copies/regular back ups & data security
 - System of adequate contingency and disaster recovery plans
 - Suggestions for improvements
 - Reconciliation of control & Subsidiary books
 - Inter branch Accounts



Certain Crucial Clauses

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- General
 - Audit/Inspection
 - Concurrent Audit
 - Internal Inspection
 - RBI Inspection
 - AFI findings
 - Previous year's reports
 - Other inspection
 - Systems Audit
 - Reporting on adverse comments in any of the above



Certain Crucial Clauses

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- General
 - Frauds
 - Occurrence
 - Timely reporting
 - Suggestions
 - Window Dressing
 - Fixed Assets relating
 - Any Other Matters



Certain Takeaways

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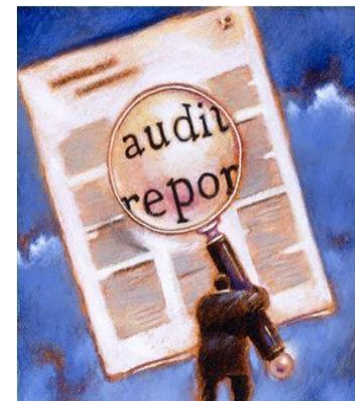
- LFAR reporting to be kept in mind while audit planning and verification of advances
- Use LFAR as checklist & List of illustrative data in GN
- Adverse remarks/ observations to be supported by instances
- Specific and clear replies not ambiguous and long
- Give annexures, if required
- Don't camouflage under provisioning or non reporting of NPA
- Random checking and Materiality (mention)
- Summary
- Discussion with branch manager before finalization

Memorandum of Changes 'MOC'



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- important document enclosed with the Bank Audit Report whenever the Auditor observes significant issues effecting the FS
- Materiality levels
- Bank Specific formats
- Discussion with management



Memorandum of Changes 'MOC'



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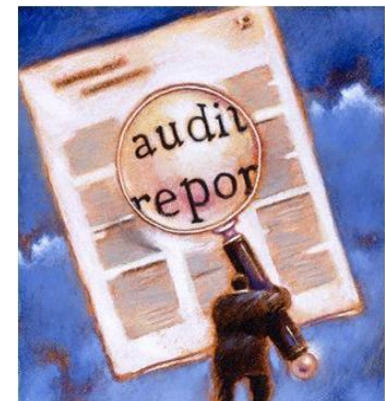
- Relating to suggested changes in Balance Sheet
- Relating to suggested changes in Profit and Loss Account
- Relating to suggested changes in advances portfolio of the bank
- Relating to outstanding balances of the advances
- Yearly return of provisions
- Details of accounts for various changes
- Reconciliation balances in interest not collected account
- Summary of advance return
- MOC for fixed assets

Memorandum of Changes 'MOC'



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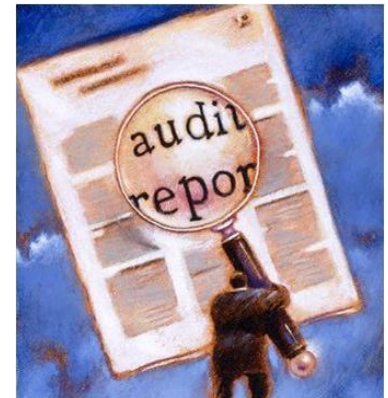




Independent Auditor's Report

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- AS per SA 700
 - Revised Format
 - Modifications (SA705)
 - Emphasis of Matter (SA706)
 - As per the Banking Regulation Act, 1949





Independent Auditor's Report

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- The following is a summary of Memorandum of Changes submitted by us to the branch management.
- **Memorandum of Changes (summary)**

<u>No.</u>	<u>Increase</u>	<u>Decrease</u>
a. In respect of Income		
b. In respect of expenditure		
c. In respect of Assets		
d. In respect of Liabilities		
e. In respect of Gross NPAs		
f. In respect of Provision on NPAs		
g. In respect of Classification of Advances		
h. In respect of Risk Weighted Assets		
i. Other items (if any)		

Jilani and Ghosh Committee Recommendations



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Jilani Committee Recommendations



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- July 1995
- Objective: to review the efficacy and adequacy of internal control, inspection and audit system in a bank with a view to strengthening the supervisory system and reliability of data.
- 3 categories of recommendations based on areas of operations – EDP, Inspection/Internal Audit & Miscellaneous.



Jilani Committee Recommendations



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- Format containing **25 questions** to be answered as “Implemented” or “Not Implemented”
- Focus on internal vigilance of the internal controls in a computerized environment
- Strength of the EDP system



Jilani Committee Recommendations



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- Follow up on major / serious irregularities detected during concurrent audit
- Fraudulent transactions reported
- Timely action to plug gaps in serious leakages
- Control measures to prevent attacks on EDP
- Regular checking of EDP
- Verification of data out put from EDP system



Ghosh Committee Recommendation

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- ❑ Accepted in 1993
- ❑ Recommendations are relating to frauds & malpractices
- ❑ Main objectives of Ghosh Committee
 - ❑ Safety of assets
 - ❑ Compliance with laid down policies and procedures
 - ❑ Accuracy and completeness of accounting and other records
 - ❑ Proper segregation of duties and responsibilities of staff
 - ❑ Timely prevention and detection of frauds and malpractices

Ghosh Committee Recommendation



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- Out of 97 – 27 applicable to branches 43 to RO/ZO/HO and balance 27 to both
- To be answered in “YES” or “NO”





Ghosh Committee Recommendation

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- ❑ Joint and Dual Custody of cash & other valuables
- ❑ Transactions in the currency Chest
- ❑ Adhering to RBI norms while issuing large payout, opening of accounts, large withdrawals
- ❑ Monthly /bi-monthly inspection of stocks pledged
- ❑ Rotation of duties amongst staff
- ❑ Financial & Admin powers to be laid down



Ghosh Committee Recommendation

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- ❑ Safe custody of unused stationery
- ❑ Granting advances beyond powers
- ❑ Instructions on phone
- ❑ Exercising of caution at the time of opening new accounts
- ❑ Safe guard of specimen signature cards
- ❑ Monitoring of inoperative accounts

Responsibility for implementation and Auditors' Role



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- Management's Responsibility
- Statutory auditor's responsibility is to verify and report on the status of implementation of these recommendations.
- A failure to comply with any of the recommendations of the two committees would be indicative of the weakness in the internal control system on the bank.



Other Certificates



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- Relating to DICGC
- Cash on hand on random dates
- Restructured Advance related
- Priority Sector Lending (MSME, Direct agriculture)
- Advances to sensitive sectors
- Movement in NPA (Provision there off)
- Claim of Interest subsidy (Education, Export & Argi)
- Rural advances, women self help groups (Interest subvention)
- PMEGP
- Off Balance sheet items

Other Certificates



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- Holding of Physical and treasury securities on behalf of HO/ other offices
- Average aggregate advances and bad debts written off
- Debt waiver (if applicable)
- Compliance of Jilani & Ghosh committees recommendations
- Textile & Jute sector, crop loans, Handloom sector etc.
- Technology upgradation fund
- Other regional state level issues/incentives



Peer Review & Quality Control

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- Documentation for audit procedures
- MRL from management
- Working papers





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