

**Hyderabad Branch
of
SIRC of ICAI**

Critical issues in Bank Branch Audit

IRAC norms

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Session Coverage

1. RBI circular dated 12.11.2021 & 15.02.2022 regarding important clarifications on IRAC norms.
2. Prudential Norms (Quick Refresher)
 - a. NPA norms
 - b. Restructuring of advances & project loans
 - c. Asset Classification
 - d. Provisioning norms

Prudential norms on IRAC and Provisioning pertaining to Advances - Clarifications

RBI/2021-2022/125 DOR.STR.REC.68/21.04.048/2021-22 Nov12, 2021

- **A. Specification of due date/repayment date**
- **B. Flagging of SMA & NPA**
- **C. Clarification regarding definition of ‘out of order’**
- **D. NPA classification in case of interest payments**
- **E. Upgradation of accounts classified as NPAs**
- **F. Income recognition policy for loans with moratorium on payment of interest**

TL sanctioned on	06-06-2020								
Amount sanctioned	1.2 crores								
Tenor	5 Years								
Repayment	60 monthly instalments of Rs 2,00,000 each commencing from							Jul-20	
Interest	10.15 %	To be paid as and when debited							

A. Specification of due date/repayment date

- ✿ The **exact due dates** for repayment of a loan, frequency of repayment, breakup between principal and interest, examples of SMA/NPA classification dates, etc. shall be clearly specified in the loan agreement.
- ✿ In cases of loan facilities with moratorium on payment of principal and/or interest, the exact date of commencement of repayment shall also be specified in the loan agreements.
- ✿ Compliance at the earliest, but not later than December 31, 2021, in respect of fresh loans.
- ✿ In case of existing loans, however, compliance to these instructions shall necessarily be ensured as and when such loans become due for renewal/review.

Prudential Framework for Resolution of Stressed Assets (PART B1)

Lenders shall identify incipient stress in loan accounts, immediately on default, by classifying stressed assets as special mention accounts (SMA) as following:

SMA sub-categories	Basis for classification – principal or interest payment or any other amount wholly or partly overdue between	For revolving credit facilities Basis for classification – Outstanding balance remains continuously in excess of the sanctioned limit or drawing power, whichever is lower, for a period of:
SMA-0	Upto 30 days	-
SMA-1	More than 30 days & upto 60 days	More than 30 days & upto 60 days
SMA-2	More than 60 days & upto 90 days	More than 60 days & upto 90 days

Default

Non-payment of debt when whole or any part or instalment of debt amount has become due and payable and is not repaid by debtor.

For revolving facilities like cash credit, default would also mean, without prejudice to the above, the outstanding balance remaining continuously in excess of the sanctioned limit or drawing power, whichever is lower, for more than 30 days.

TL sanctioned on	06-06-2020								
Amount sanctioned	1.2 crores								
Tenor	5 Years								
Repayment	60 monthly instalments of Rs	2,00,000	each commencing from	Jul-20					
Monthly due date	15th								
Interest	10.15 %	To be paid as and when debited							

December 2023 instalment not received.

When will the account be classified as SMA-0, SMA-1 & SMA-2

B. Flagging of SMA & NPA

- ✿ Borrower accounts shall be flagged as overdue by the lending institutions as part of their day-end processes for the due date, irrespective of the time of running such processes.
- ✿ **The exact due dates for repayment of a loan, frequency of repayment, breakup between principal and interest, examples of SMA/NPA classification dates, etc. shall be clearly specified in the loan agreement.**
- ✿ Classification of borrower accounts as SMA as well as NPA shall be done as part of day-end process for the relevant date and the SMA or NPA classification date shall be the calendar date for which the day end process is run. In other words, the date of SMA/NPA shall reflect the asset classification status of an account at the day-end of that calendar date. (Para 8.4)

CC limit sanctioned on		43205									
Limit sanctioned		2.5 Crores				Secured on hypothecation of stock and book debts					
						Margin 15 %					
						Deawing power as per last stock state (12-12-2023) Rs					
						2,35,56,800					
Date	Particulars	Dr		Cr	Balance						
Statement of account from 01.12.2023 to 31.03.2024											
Date	Particulars		Debit	Credit	Balance						
01-Dec-23	To Balance b/d				-1,97,00,000						
15-Dec-23	To cheques cleared		1,20,000		-1,98,20,000						
16-Dec-23	By RTGS		0	60,000	-1,97,60,000						
17-Dec-23	To cheques cleared		1,30,000		-1,98,90,000						
23-Dec-23	By RTGS			4,50,000	-1,94,40,000						
	To Cheques		8,31,000		-2,02,71,000						
29-Dec-23	To Interest		1,01,400		-2,03,72,400						
	By cash			45,000	-2,03,27,400						
	By RTGS			1,23,000	-2,02,04,400						
06-Jan-24	To TNEB		1,43,000		-2,03,47,400						
27-Jan-24	To cheques		3,85,000		-2,07,32,400						
29-Jan-24	To Interest		1,05,000		-2,08,37,400						
26-Feb-24	To Interest		1,08,000		-2,09,45,400						
07-Mar-24	By XYZ fin ltd		1,12,000		-2,10,57,400						
09-Mar-24	To cheq retd		2,50,000		-2,13,07,400						
15-Mar-24	To insp charges		1,000		-2,13,08,400						
26-Mar-24	By cheques			1,10,000	-2,11,98,400						
	To Interest		1,04,550		-2,13,02,950						
27-Mar-24	TO clearing		6,50,000		-2,19,52,950						
Summation of debit & credit			30,40,950	17,88,000							

C. Clarification regarding definition of 'out of order'

- *Covering cases where the outstanding balance in the principal operating account is less than the sanctioned limit/drawing power*
- The balance o/s is within the limit/DP, but there are no credits continuously for 90 days ~~as on the date of the Balance sheet~~
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- or the credits are inadequate to cover the interest debited during the ~~same~~ ~~period~~ previous 90 days period.

D. NPA classification in case of interest payments

✿ *In case of interest payments, banks should, classify an account as NPA only if the interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter. (Para 2.1.3 of Master circular dated Oct 01, 2021)*

CHANGED TO

✿ *In case of interest payments in respect of term loans, an account will be classified as NPA if the interest applied at specified rests remains overdue for more than 90 days.*

Facility TL	Repayment to commence	Jan-22
Instalment due by	10th of every month	
Loan	48,00,000	Last Instalment
Rol	12	Instalment
		Dec-25
		1,00,000 Per month

Statement of account from 01.04.2023 to 31.03.2024

Date	Particulars	Debit	Credit	Balance
01-04-2023	Bal B/f	35,00,000		35,00,000
20-04-2023			50,000	34,50,000
28-04-2023	Int	34,200		34,84,200
10-05-2023			90,000	33,94,200
28-05-2023	Int	34,500		34,28,700
15-06-2023	NPA 15-06-2023	0		34,28,700
15-02-2024	int	3,08,583		37,37,283
	Inst repayment		13,37,283	24,00,000
	Upgraded to STD			24,00,000
28-02-2024	int	24,000		24,24,000
15-03-2024	Inst repayment		1,00,000	23,24,000
28-03-2024	int	23,740		23,47,740

Facility TL	Repayment to commence	Jan-22
Instalment due by	10th of every month	
Loan	48,00,000	Last Instalment
Rol	12	Instalment
		Dec-25
		1,00,000 Per month

Statement of account from 01.04.2023 to 31.03.2024

Date	Particulars	Debit	Credit	Balance	DP as on 15th	overdue
01-04-2023	Bal B/f	35,00,000		35,00,000	32,00,000	Apr-23 3,00,000
20-04-2023			50,000	34,50,000	31,00,000	May-23 2,94,200
28-04-2023	Int	34,200		34,84,200	30,00,000	Jun-23 4,28,700
10-05-2023			90,000	33,94,200	29,00,000	Jul-23
28-05-2023	Int	34,500		34,28,700	28,00,000	Aug-23
15-06-2023	NPA 15-06-2023	0		34,28,700	27,00,000	Sep-23
15-02-2024	int	3,08,583		37,37,283	26,00,000	Oct-23
	Inst repayment		13,37,283	24,00,000	25,00,000	Nov-23
	Upgraded to STD			24,00,000	24,00,000	Dec-23
28-02-2024	int	24,000		24,24,000	23,00,000	Jan-24
15-03-2024	Inst repayment		1,00,000	23,24,000	22,00,000	Feb-24 2,00,000
28-03-2024	int	23,740		23,47,740	21,00,000	Mar-24

E. Upgradation of accounts classified as NPAs

- ✿ it is clarified that loan accounts classified as NPAs may be upgraded as ‘standard’ asset only if **entire arrears of interest and principal** are paid by the borrower.
- ✿ With regard to upgradation of accounts classified as NPA due to restructuring, non-achievement of date of commencement of commercial operations (DCCO), etc., the instructions as specified for such cases shall continue to be applicable.

F. Income recognition policy for loans with moratorium on payment of interest

- ✿ Loans where moratorium has been granted for repayment of interest, lending institutions may recognize interest income on accrual basis for accounts which continue to be classified as ‘standard’.
- ✿ However loans with moratorium on payment of interest (permitted at the time of sanction of the loan) become NPA after the moratorium period is over, the capitalized interest corresponding to the interest accrued during such moratorium period need not be reversed.

Prudential norms on IRAC and Provisioning pertaining to Advances – Further Clarifications

RBI/2021-2022/158 DOR.STR.REC.85/21.04.048/2021-22 Feb 15, 2022

A. Out of Order Definition –applicable to all loan products offered as overdrafts including those for non business purpose and / or which entails interest repayments as only credits

B. Previous 90 days period –in Out of Order inclusive of the day for which the day-end process being run.

C. More than one facility –Upgrade to standard asset on repayment of entire arrears-int. & principal of all credit facilities.

D. No changes on CRILIC reporting requirements

Prudential Norms

A Quick Refresher

NPA NORMS

- Uniform norm of 90 days for all advances including Government guaranteed Accounts
- Agricultural loans – Continues to be based on crop seasons

NPA NORMS- Term Loans

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- Instalments of principal remain overdue for a period of more than 90 days in respect of a term loan.
- In case of interest payments in respect of term loans, an account will be classified as NPA if the interest applied at specified rests remains overdue for more than 90 days

NPA NORMS- Term Loans

- If **arrears** of interest and principal are paid by the borrower in the case of loan accounts classified as NPAs, the account should no longer be treated as non-performing and may be classified as ‘standard’ accounts. (**Para 4.2.5 – RBI Master circular**).
- Upgradation is allowed only if the account reaches “no overdues” status. This should not be misunderstood with “overdues brought within 90 days”. (**ICAI GN – Para 11.139 Page 478**)

NPA NORMS- OD/CC

- The account remains 'out of order' in respect of an Overdraft/Cash Credit (OD/CC).
- An account should be treated as '**out of order**' where
 - The balance o/s in the account remains continuously in excess of the limit/DP during a period of 90 days.
 - The balance o/s is within the limit/DP, but there are no credits continuously for 90 days ~~as on the date of the Balance sheet~~
 - or the credits are inadequate to cover the interest debited during the ~~same~~ ~~period~~ previous 90 days period.

NPA NORMS - Bills

- A bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.

Agricultural Advances- NPA

- A loan granted for short duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for two crop seasons.
- A loan granted for long duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season.
- “Long duration” crops would be crops with crop season longer than one year
- Crops, which are not “long duration” crops, would be treated as “short duration” crops.
- The crop season for each crop, which means the period up to harvesting of the crops raised, would be as determined by the State Level Bankers’ Committee in each State.

Agricultural Advances- Interest application

Examples of Interest application according to crop seasons and for other activities:

Crop Season	Kharif	Rabi
Disbursement Period	April 01 to September 30	October 01 to March 31
Interest Application Date	Due date fixed for repayment	Due date fixed for repayment
Compounding from date	After due date	After due date
Penal Interest	From date the loan becomes overdue	From date the loan becomes overdue

Refer page
388 of ICAI
GN

Agricultural Advances- Interest application

	Allied Activities	
	Dairy, Poultry	Goat Rearing, Piggery
Repayment	Quarterly	Half Yearly / Yearly
Interest Application	Quarterly	Half Yearly / Yearly
Interest application date	Quarter end	Half Year end / Year end
Compounding Frequency	Quarterly	Half Yearly / Yearly
Compounding from date	After Quarter end	After Half Year end / Year end
Penal Interest	If overdue, after Quarter end	If overdue after half year /year end.

Crop Season- RBI clarification recd by Maharashtra SLBC

- Loan may be treated as NPA immediately on completion of two crop seasons / one crop season (as the case may be, depending on the duration of the crops) after the repayment due date.
- Two crop seasons after the due date should refer to only those two consecutive crop seasons in which the farmer usually undertakes crop production.

RBI clarification – Crop season

The crop season for each crop, means the period up to harvesting of the crops raised. The asset classification norms assume that there is normal crop yield during the season for which credit is extended.

Hence, immediately after consecutive two harvest seasons (as per the cultivation pattern followed by the farmer borrower) from repayment due date, the account is to be identified as NPA.

In case of natural calamities as declared by the SG, the loan should be restructured/ rescheduled

Agri loan NPA - Examples

S.No.	Particulars	Short Term Crops		Long Term Crops	
		Kharif	Rabi	Sugarcane	Banana
1	Sanction date	1 st April 2020 to 30 th September, 2020	1 st October 2020 to 31 st March, 2021	1 st October, 2019	1 st July, 2019
2	Harvesting time	September, 2020	March, 2021	December, 2020	September, 2020
3	Repayment due date	31 st December, 2020	30 th June, 2021	31 st March, 2021	31 st December, 2020
4	Interest subvention @ 3%	Available upto the date of repayment subject to maximum repayment due date.(subject to 1 year)	Available upto the date of repayment subject to maximum repayment due date. (subject to 1 year)		
5	Date of irregularity	31 st December, 2020	30 th June, 2021	31 st March, 2021	31 st December 2020

Refer page
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GN

Agri loan NPA - Examples

<u>Multiple/ double cropping pattern</u>					
6	First crop season end date	30 th June, 2021	31 st December, 2021	NA	NA
7	Second crop season end date	31 st December, 2021	30 th June, 2022	NA	NA
8	Date of NPA	31 st December, 2021	30 th June, 2022	NA	NA
<u>Single/ mono cropping pattern</u>					
9	First crop season end date	31 st December, 2021	30 th June, 2021	31 st March 2023	31 st December 2022
10	Second crop season end date	31 st December 2022	30 th June, 2022	NA	NA
11	Date of NPA	31 st December 2022	30 th June, 2022	31 st March 2023	31 st December 2022

Agri – NPA Examples for allied activity

Allied Activity (Instalment)				
Type	Dairy	Goat Rearing	Piggery	Poultry
	(equated quarterly instalment with moratorium period, first instalment is due on Sept 30, 2020)	(equated half yearly / yearly instalment considering moratorium period of six months first instalment is due on June 30 2021)	(equated half yearly / yearly instalment considering moratorium period of six months first instalment is due on June 30, 2021)	(equated quarterly instalment with moratorium period, first instalment is due on Sept 30, 2020)
Loan Disbursed	1-Jun-2022	1-Jul-2021	1-Jul-2021	1-Jun-2022
Due Date	30-Sep-2022	30-Jun-2022	30-Jun-2022	30-Sep-2022
Overdue Date	30-Sep-2022	30-Jun-2022	30-Jun-2022	30-Sep-2022
Compounding	30-Sep-2022	30-Jun-2022	30-Jun-2022	30-Sep-2022
NPA turning date	30-Dec-2022	29-Sep-2022	29-Sep-2022	30-Dec-2022
Remarks	NPA upon running day-end process on 90 days overdue	NPA upon running day-end process on 90 days overdue	NPA upon running day-end process on 90 days overdue	NPA upon running day-end process on 90 days overdue

Agricultural Advances

- Where natural calamities impair the repaying capacity of agricultural borrowers, banks may decide on their own as a relief measure conversion of the short-term production loan into a term loan or re-schedulement of the repayment period; and the sanctioning of fresh short-term loan, subject to guidelines contained in
- Master Direction – Reserve Bank of India (Relief Measures by Banks in Areas affected by Natural Calamities) Directions 2018 – SCBs dated October 17, 2018, as updated from time to time.

Significant factors for classifying an account as NPA in Working capital advances

- Stock statements should not be more than 3 months old.
- Regular and ad hoc limits should not be left lapsed without renewal for a period of more than 180 days
- Solitary or very few credits in the account before the balance sheet date.

Prudential Framework for Resolution of Stressed Assets

- **RBI has announced a revised framework for resolution of stressed assets on June 07, 2019.** (RBI/2018-19/203 DBR.No.BP.BC 45/21.04.048/2018-19

Framework aims at strengthening the structure by:

- 1) Early identification and reporting of stress
 - 2) Implementation of resolution plan for defaulting accounts, supported by independent credit evaluation by credit rating agencies.
 - 3) Implementation conditions have been prescribed.
 - 4) Enable banks to take timely action for resolution of stressed accounts & provides for adequate disclosures by banks
 - 5) Additional provision if RP not implemented within prescribed timelines.
 - 6) Envisages higher provisioning, penal action & direction to file under IBC on banks in case of concealing of information.
- **The revised framework has discontinued with immediate effect Framework for Revitalising Distressed Assets, CDR, Flexible Structuring of Existing Long Term Project Loans, SDR, Change in Ownership outside SDR, and Scheme for Sustainable Structuring of Stressed Assets. Joint Lenders' Forum (JLF) as mandatory institutional mechanism for resolution of stressed accounts also stands discontinued**

Meaning of Restructured Account

- Reserve Bank of India has defined a restructured account as one where the bank, for economic or legal reasons relating to the borrower's financial difficulty, grants to the borrower **concessions** that the bank **would not otherwise consider**

Meaning of Restructured Account

- Restructuring means **modification** of terms of the advances including **alteration**
 - in repayment **period**, (including extension of moratorium period)
 - repayment **amount**,
 - amount of installments,
 - **rate of interest**.

When is implementation complete?

- All related documentation, including execution of necessary agreements between lenders and borrower / creation of security charge / perfection of securities are **completed by all lenders**; and
- The new capital structure and / or changes in the terms and conditions of the existing loans get duly reflected in the books of **all the lenders and the borrower**.

Restructured Accounts- Key points

- **Specified Period** means a period of one year from the commencement of the first payment of interest or principal, **whichever is later**, on the credit facility with longest period of moratorium under the terms of restructuring package.
- Satisfactory performance during the specified period means adherence to the specified conditions during that period.

Restructured Accounts- Key points

Satisfactory performance

Non-Agricultural Cash Credit Accounts

- In the case of non-agricultural cash credit accounts, the account should not be out of order any time during the specified period, for duration of more than 90 days and there should not be any overdues at the end of the specified period.

Non-Agricultural Term Loan Accounts

- In the case of non-agricultural term loan accounts, no payment should remain overdue for a period of more than 90 days and there should not be any overdues at the end of the specified period.

All Agricultural Accounts

- In the case of agricultural accounts, at the end of the specified period the account should be regular.

Project Loans

- **Project loans** is the long-term finance of infrastructure and industrial projects based upon the projected cash flows of the project rather than just the balance sheets of its sponsors.
- the '**Date of Completion**' and the '**Date of Commencement of Commercial Operations**' (**DCCO**), of the project should be clearly spelt out at the time of financial closure of the project and the same should be formally documented.

Project Loans

- In several instances, the completion of the projects is delayed due to extraneous reasons beyond the control of the promoters.
- The reasons for delay include legal disputes, delay in obtaining government approvals, etc.
- In such a situation Banks may restructure / reschedule
 - Project loans for infrastructure sector
 - Project loans for non infrastructure sector

Project Loans

Deferment of DCCO not treated as restructuring and hence asset classified as Standard

Infrastructure Projects	Non Infrastructure Projects	Conditions
The revised DCCO falls within a period of two years from the original DCCO stipulated at the time of financial closure	The revised DCCO falls within a period of one year from the original DCCO stipulated at the time of financial closure	The revised repayment period should be equal to or shorter than the original repayment term. In other words if the repayment term is extended it will amount to restructuring

Standard Asset - Provision required 0.40%

Restructuring of Project loans by way of revision of DCCO for reasons beyond the control of the promoters

Infrastructure Projects	Non Infrastructure Projects	Conditions
Up to another one year (total extension of three years from the date of original DCCO).	Up to another one year (total extension of two years). Please note that this benefit is not available to Commercial Real Estate Exposures	1. The application for restructuring should be received before the expiry of the deferred DCCO & the account must be standard as on the date of application for restructuring 2. In case of moratorium for payment of interest, banks should not book income on accrual basis beyond two years (for infrastructure loans) & one year (for non infrastructure loans) from the date of original DCCO

Standard Asset - Provision required 5.00%

Restructuring of Infrastructure Projects involving court cases

Infrastructure Projects	Conditions
Up to another two years (total extension of four years from the date of original DCCO), in case the reason for extension of DCCO is arbitration proceedings or a court case.	<ol style="list-style-type: none">1. The application for restructuring should be received before the expiry of the deferred DCCO & the account must be standard as on the date of application for restructuring2. In case of moratorium for payment of interest, banks should not book income on accrual basis beyond two years (for infrastructure loans) & one year (for non infrastructure loans) from the date of original DCCO

Standard Asset - Provision required 5.00%

Word of Caution ...

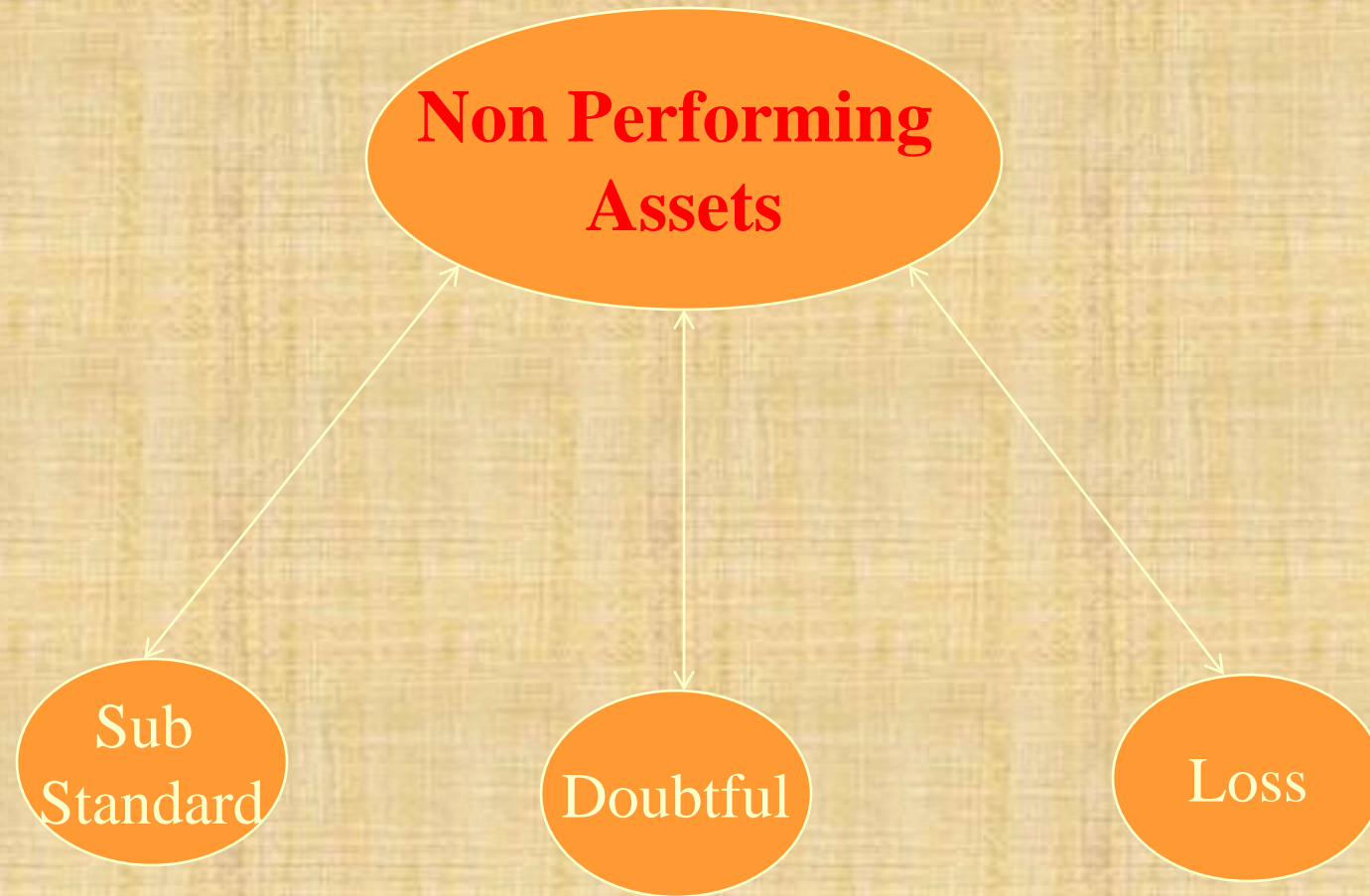
- ❖ Not all accounts can be considered for this Project Loan Treatment
- ❖ Auditors to verify the eligibility criteria clearly with the relevant circulars
- ❖ In case not classifiable, the special treatment will have to be withdrawn

Income Recognition

- Income is to be recognised based on recovery
- Not applicable to advances against Life Insurance Policies, NSCs, IVPs, KVPs etc, provided requisite margin is maintained.
- Critical area in respect of OD against deposits wherein Deposits with multiple Interest are taken as security
- Critical area in respect of loan against FD wherein interest is drawn periodically by the depositor but interest on loan is accumulated without payment

Reversal of Interest

- In respect of accounts classified as NPA for the first time, interest debited in the current year (2023-2024) and **previous years** which has not been realised should be reversed or provided.
- This will apply to Government guaranteed accounts also.



Sub Standard Assets & Doubtful assets

- An NPA which is less than 12 months old – SSA
- An NPA which is more than 12 months old - DA
- In case erosion in value of securities is more than 50%, classify as doubtful
- Critical point – Valuation has to be done once in three years for NPAs.

Loss Assets

- An asset considered uncollectible
- An asset where **loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly**
- An asset whose security value has been eroded by more than 90 % of the advance value

Asset Classification

- Asset Classification to be borrower-wise and not facility-wise

Exceptions

- Bills discounted under LC until default
- Mark to market value of derivatives contract
- Additional facility granted to a restructured NPA

Asset Classification

- Asset classification of **accounts under consortium** should be based on the record of recovery of the individual member banks
- In case of multi branch financing – The classification by the branch where main limit is availed has to be considered by all branches.
- **CRITICAL** – Certificate from Main branch is compulsory since the operations may be good in the branch where sublimit is availed.
- A NPA need not go through the various stages of classification in cases of serious credit impairment

Asset Classification

- **Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and life policies need not be treated as NPAs.**
- Advances against gold ornaments, government securities and all other securities are not covered by the above exemption
- A sub-standard accounts which has been subjected to restructuring etc., would be eligible to be upgraded to the standard category only after the specified period of one year

Asset Classification

Govt. Guaranteed Accounts

Accounts to be classified as NPA if guaranteed by

- Central Govt. when the guarantee is repudiated.
- State Govts. When the guarantee is invoked and remains in default for more than 90 days.

Provisioning Whose responsibility

- *The primary responsibility for making adequate provisions for any diminution in the value of loan assets, investment or other assets is that of the bank managements and **the statutory auditors.***
- *The assessment made by the inspecting officer of the RBI is furnished to the bank to **assist the bank management and the statutory auditors** in taking a decision in regard to making adequate and necessary provisions in terms of prudential guidelines.*

Provisioning Norms

Standard assets(other than Restructured accounts) – on global loan portfolio

- | | |
|--|--------------|
| a) Direct advances to agricultural and SME sectors | 0.25% |
| b) Commercial Real Estate (CRE) Exposures | 1 % |
| c) Commercial Real Estate – Residential Housing Sector (CRE-RH) | 0.75% |

Provisioning Norms

- Standard assets (other than Restructured accounts) – on global loan portfolio
- d) Housing loans extended at teaser rates – 2%
(The provisioning on these assets would revert to 0.40per cent after 1 year from the date on which the rates are reset at higher rates if the accounts remain ‘standard’.)
- e) All other Standard advances – 0.40%

Accounts Restructured during the current year classified as standard – 5 %

Provisioning Norms

- Sub standard assets - 15 percent on total outstanding should be made without making any allowance for DICGC/ECGC guarantee cover and securities available

Substandard Assets

- In case of Substandard accounts, where security available abinitio at the time of sanction is less than 10% of both funded and non funded limits put together, then the provision to be made is 25 % **(20% in case there is an escrow account in case of infrastructure lending, infrastructure loan accounts)** of the Outstanding Value
- It is different from erosion of security to be classified as loss asset.

Provisioning Norms

- Doubtful assets – 100 % of the unsecured portion
+
25/40/100% (depending on age) of the secured portion
- Loss Asset – 100%

PROVISIONING – 2023-2024

Sl. No.	NPA Date	Status of Asset	Unsecured Portions	Secured Portion
I	Before 1.4.2020	D3 – Current year	100% of Outstanding irrespective of the availability of security as reduced by ECGC cover	

II	1.4.2020- 31.3.2022	D2 – Current year	100% as reduced by ECGC Cover	40%
III	1.4.2022- 31.3.2023	D1 – Current year	100% as reduced by ECGC Cover	25%
IV	1.4.2023- 31.3.2024	Substandar d current year	15% of the outstanding irrespective of security or ECGC Cover **	

Master Circular Ref

- **RBI/2023-24/06 DOR.STR.REC.3/21.04.048/2023-24 dated April 01, 2023- Master circular for Prudential norms on IRAC and Provisioning relating to Advances**

THANK YOU



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Planning an effective Bank Branch Audit & Frauds in banking

ICAI - Hyderabad Branch
(SIRC)

20 March 2024

CA. Ketan Saiya

FCA, DISA (ICAI)



Coverage ...

- ➡ **INTRODUCTION / BASICS**
- ➡ **AREAS OF AUDIT**
- ➡ **EXECUTION & DOCUMENTATION**
- ➡ **EFFECTIVE REPORTING**
- ➡ **LATEST PICKS**



Overall Development

- Reduction in Audit limits
- 2 Branch per auditor

- 12 PSU Bank
- 22 Private Banks
- 46 Foreign Banks
- 56 RRB
- 12 Small Finance Banks
- 6 Payment Banks
- 1485 Urban Co-op
- 96,000 Rural Co-op
- NBFCs



AUDIT - INTRODUCTION

Introduction ...

- Expectation / coverage / Risk is very high in bank audits & Time is biggest constrain.
- There have been limitations in reporting in some banks by giving limited options in online reporting which needs to be reported

AUDIT - INTRODUCTION

- To meet Deadlines of Reporting
- Well equipped and knowledgeable Team
- Attendance is compulsory, obtain certificate of attendance
- Frauds / Early warning signals of frauds in advances

Benefits

- Updated with Latest Happening in Banking
- To learn about New Industry

BASICS....

- Compliance with BR Act & RBI Guidelines
- Compliance with Policies of Bank
- Guidance Note of ICAI
- Go thru Standards on Auditing like -
 - Knowledge of Business,
 - Terms of Audit Engagement,
 - Audit Planning,
 - Audit Sampling,
 - Audit Documentation
 - Audit Evidence
 - Using the work of another auditor, Audit Materiality

Obtaining Information ...

- Read Appointment Letter - Terms Conditions very Carefully.
- Size of branch- Advances & Deposits,
- To Know Branch Timing & Match it
- Name / Portfolio and Designation of staff.
- Obtain All Telephone/ Fax numbers / Email id
- Issue Requirement letter
- List the requirements i.e. report and certificates to be signed. E.g. Quarterly some additional returns are to be signed

Introduction...

- Obtaining the list of Reports Generated by Computer system.
- List of books and records maintained manually.
- Obtain latest reports i.e. Statutory Auditors and internal reports to H.O.
- Obtain monthly average of advances and deposits, E.g. XYZ Bank Matunga
- Review accounting policies and auditors report of the bank
- Obtain H.O. Latest RBI Circulars

Statutory AUDIT - INTRO...

- Prepare Audit programme
- Define Audit Procedures - Extent / Periodicity of Checking.
- Documentation to be created.
- Define Materiality Levels
- Representation letter / Confirmations to be obtained.
- Discuss the Draft Reports- reservation, major observation, qualifications with branch management.

➤ .

Introduction...

- To Quantify the Qualification. E.g. Error in Interest Calculations / Non-charging of penal interest, Other Revenue leakages.
- Issue of final reports in Time.
- Provisioning of expenses in March.
- Rent expenses.
- Security aspect in NPA advances.

Introduction...

Team to have Knowledge of :

- Function of bank
- Banking Industry - Rules & Regulations applicable
- Products handled by Bank
- If Forex Branch, FEDAI Guidelines - Foreign exchange transactions

Introduction...

- Team needs to be fully conversant with the nitty gritty and possess adequate knowledge to counter the defensive arguments put forth by the branch.
- Have Practice of Giving Queries in writing & Taking acknowledgement
- Seniors to Review queries and replies on regular basis so the report review and discussion is easy.

BASIC...Planning...Staff

- ⇒ Identify the staff -
 - ⇒ Experienced/Train the staff (CBS system)
 - ⇒ Access to CBS and other arrangements
 - ⇒ Manpower requirement -
 - ⇒ *Allocate the work* (Deposits, Advances, Misc. items, etc.), decide who does what?
 - ⇒ How many days/hours, time to be spent on monthly reporting
- ⇒ **Timely Completion of the checking and report**

EXECUTION OF WORK

- Obtaining Audit Evidence
- Audit working papers - complete
- Timely discussion and rectification of queries
- Exhaustive Checklist - Provided by banks / Develop In house

CHECKLISTS...

Few Exceptional reports

- Overdrawing
- Debits in in-operative accounts / SB a/cs
- Operation in In-operative Accounts.
- Cash transactions without PAN
- Overdue amounts
- TOD accounts
- TOD's in CA & SB accounts
- Cheque/s drawn against clearing accounts

Reporting to Management/RBI

- In case Fraud detected during the audit, issue Flash Report to Management
- Any transaction susceptible to fraud should be directly reported to RBI by the Auditor and to the top management

Imp of Documents

- Audit not documented is audit not done
- Peer Review
- Regulatory Bodies calling documents / information
- Frauds



Why Documentation plays a Crucial Role in Audit today?

- Documentation ensures regulatory compliance, minimizing non-compliance risks and penalties.
- Transparent Documentation fosters accountability, tracing financial activities accurately.
- Documentation aids auditors in assessing the bank's risk exposure accurately.
- Allows auditors to identify potential risks, such as fraud, operational errors, or inadequate internal controls, enabling proactive risk mitigation strategies.



Essential Documents in Bank Branch Audit

- Engagement Letter
- Balance Sheet, Profit and Loss Account
- Long Form Audit Report
- Management Representation Letter
- Attendance Certificate - Ratnagiri



As per Guidance Note Below Docs to be collected

1. Trial Balance as on 31st 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. List of certificates required to be certified by the branch auditor.
3. Review of previous years auditor report / LFAR.
4. Latest RBI master directions ` for "Income recognition and assets classification" & other relevant circulars.
5. List of comments of RBI inspection report towards the branch.



As per Guidance Note Below Docs to be collected

6. Latest branch concurrent audit report / Internal inspection report/ Diligence Report / Credit 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.
9. Working papers on actual audit engagement carried out for the year
10. testing of internal controls and other operational issues at the branch
11. Review of Ghosh and Jilani committee Recommendations.



As per Guidance Note Below Docs to be collected

12. Fixed Assets:

- Fixed Assets register as on 31st 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 31st March.

13. Bank reconciliation:

- List of bank account which branch maintained with other banks.
- Reconciliation statement of all banks account as on 31st march.



As per Guidance Note Below Docs to be collected

14. Inter branch reconciliation:

- Inter branch reconciliation statement.
- Provision for net outstanding debit balance for more than 6 months (refer RBI Circular DBOD No.BP.BC.73/21.04.018/2002-03 dated February 26, 2003 on Inter-branch Accounts -Provisioning for net debit balance).
- Review of inter office ledger accounts classified under other assets and other liabilities

15. Cash

- Physical cash balance verification during branch audit period (cash on hand as well as cash at ATM, if applicable).
- Report of the physical cash verification conducted by branch on 31st March.

16. Liabilities

- Verification of current/ savings accounts, term deposits including KYC, PMLA, FEMA and other compliances

Gold Loan

- Process of Gold Sanction
- Valuations Report
- Fake Gold / ornaments issues
- Loans closed & opened on same day



Some Picks..

2 booked for ₹86 lakh cash fraud in Karnal

- Police in Karnal on Friday booked two employees of an ATM cash loading company for an alleged cash fraud worth ₹86 lakh.
- They allegedly misappropriated the cash while loading it in different ATMs of the town, police said.
- The misappropriation of the money came to light during the internal audit of the company, they added.



Issues in Home loan

- ITR manipulation
- No flat available
- No borrower available
- Fake documents submitted - color xerox
- Arrangements to keep builder account standard



Fixed deposit fraud in banks

- Police said the accused approached the trusts and individuals to open FDs with public-sector banks using middlemen.
- In rete of interest. Once the FD was opened, the accused gave fake receipts to the entities and used the original ones to open accounts with forged documents.
- They then transferred the overdraft amount to their accounts using the real-time gross settlement system facility...

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Thank You



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