

NOTE ON BACKGROUND MATERIAL

The objective of the background material is to provide guidance/instructions/reference material to auditors in the conduct of audit of a Bank Branch for the year 2007-08, to enable them to be equipped with the basic knowledge and skills and to ensure that the assignment is completed expeditiously and in the manner expected.

Besides the statutory, regulatory and accounting compliances in connection with the issuance of the Main report, the Long form Audit Report and Tax Audit Report, there are several other certificates/attestations which now form the scope of Branch Auditor's work.

It becomes imperative that the entire scope of work (covered by the appointment letter), involving voluminous work and extensive procedures, is understood and the entire assignment is well planned and executed, without sacrificing quality; and so that all requisite reports/attestations are furnished within the stipulated severe time constraints imposed for the completion of the assignment.

The background material is covered in **Sections A to O**, which are dealt with briefly hereunder.

On acceptance of appointment as Branch Auditor, it is recommended that he issues, to the Branch Management, communications (text of which is recommended in **sections A and B**) covering his requisition for the financial statements, information and explanations basically required for the purpose of his assignment; and while these communications are self explanatory, these and the audit procedures could be further strengthened/ supplemented modified/ by any other additional requirements necessitated by matters/issues specifically known to the Branch Auditor (if he is familiar with the Branch affairs/operations by virtue of his having been the auditor in the past or otherwise). Since audit procedures warrant that responses and Management representations to these communications form part of the work papers/ documentation/ evidence to be preserved and used to support the audit observations / opinions/ conclusions such responses should, therefore, be received **in writing**; and so that these are duly considered by the auditor, these should be not be cryptic or evasive.

The assignment culminates in reports/certificates/attestation and to take care of the qualitative aspects of these, it is recommended that the Branch Auditor should follow the procedures as per **Section C** and keep in view matters deserving attention in Annexures C1 to V.

The recommended Audit Programme, supplemented by additional/extended procedures, if any, that may be required as the audit progresses, must be completed and retained as evidence of work executed by audit staff.

While examining the financial statements, due importance needs to be given to all heads of accounts, based on the audit risk attached thereto, and as covered by the recommended Audit Programme, special emphasis is invariably required for verification of the Advances portfolio, in respect of which auditors have greater responsibility, since provisions in respect thereof are to be to their satisfaction.

To familiarise auditors with the prudential norms applicable in relation to the Advances portfolio (for income recognition, asset classification and provisioning), a gist of the Master Circular issued on 1.07.2006 by the Reserve Bank of India (RBI) is incorporated in else where and could be used as a basic reference material. It is recommended that in respect of each large borrower, information be obtained in a structured format (Refer Section A III) which not only would cover the reporting requirements of the LFAR, but also serve the purpose of incorporation in the Main Report, any observations that affect classification/income recognition and provisioning. In response to the LFAR questionnaire, such form duly completed for each large borrower (by the branch and verified by the auditor), could be annexed to that report.

It is expected that each bank would issue its own

Circulars/instructions giving effect to, and covering compliance of RBI guidelines/directives; and that these would be available to the branch/auditors in connection with audit. These (and particularly the year end "Closing of Accounts" circular usually issued by each bank) may be sought and referred to.

The importance of Internal Controls (**Schedule H**) and analytical procedures (**Section I**), cannot be ignored and have been briefly touched upon. It was also deemed necessary to briefly touch on the extended scope of work relating to reporting on frauds (**Section K**), Fringe Benefit Tax (**Section L**) and the Banking Cash Transactions Tax (**Section M**), for guidance to the auditors. Reference may also be made to the form and manner of reporting compliance of the Ghosh and Jilani Committee requirements, by way of a negative assurance certificate (**Section O**).

While at the Branch level, it may not be relevant, it is important that the Auditors understand the regulatory requirements as regards **various disclosures in the case of Banks**; and the importance of correctness and completeness of the information both at the centralized and the decentralized levels. These have been summarized in **Section N**.

Accounting/ Auditing and Assurance Standards

In performing his duties, besides knowledge of the Accounting Standards and their applicability, the auditor must be fully conversant with the Auditing and Assurance Standards as these are mandatory in nature: and attention is drawn also to AAS 20 (as regards knowledge of banking business) and AAS 21(Consideration of Laws and Regulations in an Audit of Financial Statements) and for the letter he must enquire and be satisfied that the Branch maintains a record/register of the applicable statutes/regulations and has updated them for compliance, as a system. (Refer **section G, G I and II**)

Reports

Recommended forms of the Main (Statutory) Reports are given in **Section D** (for Nationalised Banks), **Section DD** (for Banking Companies), with some illustrative comments/observations/qualifications in **Section D.Q**; and subject to any specific formats of annexures/schedules recommended by the individual banks, the ones given in the background material are suggested to be followed. The objective of giving the form/text of the report, is to ensure compliance of audit reporting requirements as well as to emphasise that the report needs to unambiguous, complete and clear in conveying what is expected to be reported. Information which is factually correct (and not means of information), must be ensured and the **concept of materiality must be kept in view**. Matters affecting statutory responsibilities of auditors as well as non-compliance with the Statements and Standards issued by the Institute of Chartered Accountants of India (also refer to **Section G**) must be incorporated in the Main Report, while others [(including the responses to the Long Form Audit Report (LFAR) questionnaire (**Section F**)] must be given in that report. Long Form Audit Report (**LFAR**) should not be treated as a substitute for the Main Report.

Other Certificates/ attestation

In giving other certificates/attestations, the Auditor needs to satisfy himself as to the factual information and the level of assurance that he can take responsibility for. Circumstances may warrant a negative assurance in some cases (e.g., as in case of the attestation in Section O).

It is hoped that the Audit Programme and other guidance/instructions given in the background material will assist in the expeditious completion of the assignment and will also enable the auditor to prepare meaningful and effective reports in the manner expected.

March ___, 2008

The Manager

_____ Bank
_____ (Branch)

URGENT

Dear Sir,

Sub: Audit of your Branch for the year 2007-2008 – Audit engagement/ Management representations:

You have already been informed by your Management that we have been appointed as the auditors to audit and report on the accounts of the Branch for the year 2007-08.

We have accepted the appointment, and we confirm that the audit shall be carried out in accordance with the applicable legal provisions and the regulatory requirements, besides the applicable authoritative pronouncements of the Institute of Chartered Accountants of India, with the objective of expressing an opinion on the Branch financial statements. For this purpose we will perform sufficient tests to obtain reasonable assurance as to whether the information contained in the accounting records and other source data is reliable and sufficient as the basis of the preparation of the financial statements; and whether the information is properly presented in the said statements.

We wish to clarify that the responsibility for the preparation of the financial statements including adequate disclosure is that of the Management, and this includes the maintenance of adequate accounting records and internal controls, the selection and consistent application of appropriate accounting policies, including implementation of applicable accounting standards along with proper explanation relating to any material departures from those accounting standards. The management is also responsible for making judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the Branch at the end of the financial year and of the profit or loss of the Branch for that period, and the safeguard of the assets of the Bank/branch.

We will conduct our audit in accordance with the auditing standards generally accepted in India and with the requirements of law. Those Standards require that we plan and perform the audit

to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting

principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

However, having regard to the test nature of an audit, persuasive rather than conclusive nature of audit evidence together with inherent limitations of any accounting and internal control system, there is an unavoidable risk that even some material misstatements of financial statements, resulting from fraud, and to a lesser extent error, if either exists, may remain undetected.

In addition to our report on the financial statements, we expect to provide you with a separate letter concerning any material weaknesses in accounting and internal control systems which might come to our notice through the Long Form Audit Report (LFAR), or otherwise.

The responsibility for the preparation of financial statements on a going concern basis is that of the management.

We also wish to invite your attention to the fact that our audit process is subject to 'peer review'

BANK BRANCH AUDIT (2007-2008)

under the Chartered Accountants Act, 1949. The reviewer may examine our working papers during the course of the peer review.

As part of the audit process, we will expect to receive from the Management, written confirmation of the representations made to us.

We wish to complete some audit procedures even prior to the year-end, depending on your state of readiness/response.

In view of the severe time constraints imposed, we are confident you will make available to us, within the dates stipulated, the Branch returns/statements **duly completed, pre- reviewed and duly authenticated**, to enable us to furnish our reports in the form and manner desired of us by law or by the Reserve Bank of India and not necessarily in the form and manner prescribed by the Bank.

The Branch returns on which we are expected to furnish our reports, would be the financial statements that correspond to:

- (a) the Balance Sheet as at 31.3.2008;
- (b) the Profit and Loss Account for the year 2007-08;
- (c) the statements relating to the particulars of Advances as at 31.3.2008; and
- (d) other supporting returns/statements/annexures (including those as per Annexure A.1, covering also the LFAR requirements).

Please ensure that all the returns, statements and schedules are complete in all respects and are authenticated by the authorised signatories and handed over to us on the 1.4.2008. It is imperative that we also have your confirmation by 1.4.2008, that you would be meeting this commitment, to enable us to plan our audit exercise. **We await your commitment.**

To enable us to monitor the progress of the audit and completion of the assignment, please indicate/mention, the actual date(s) of completion as well as handing over to us of each statement/return/confirmation required to be prepared by you (as per the contents of the letter of appointment sent to us), by your endorsement on each such statement/return/confirmation; as also on the management representation letter required to be furnished by you to us. This is imperative for our record and necessary action.

In order to enable us to finalise and furnish our report on the audit of the accounts for the said year of your Branch, may we request you to provide the information/clarifications as stated in **Annexure 'I'** to this letter.

A written response (para-wise), to our requirements is imperative, and such response is to be based on your verification of facts.

Please note that we shall be in a position to take up the audit of the financial statements for the purpose of our report, only upon completion by you, in its entirety, of all the returns/ schedules/ statements/information sought, and upon receipt of your response in writing to this communication.

We shall be grateful if you could confirm the name(s) of the Officer(s) designated by the Branch to comply with our requirements in connection with the audit, so that our reports are expedited.

We shall appreciate your co-operation in the matter.

Thanking you,

Yours faithfully,

CHARTERED ACCOUNTANTS

ANNEXURE - I

Annexure I to letter dated March _____, 2008

INFORMATION /REQUIREMENTS IN CONNECTION WITH THE AUDIT OF ACCOUNTS FOR THE YEAR ENDED MARCH 31, 2008

1. Latest Reports:

For our scrutiny, the following **latest reports** on the accounts of your Branch, **and compliance by the Branch** on the observations contained therein:

- (a) Branch Audit Report and Accounts;
- (b) Long Form Audit Report;
- (c) Internal Inspection Report;
- (d) Internal/Concurrent Audit Report(s)/Credit Audit Report;
- (e) RBI Inspection Report, if such inspection took place;
- (f) Income and Expenditure Control Audit/Revenue Audit Report;
- (g) Quarterly review report (compliance);
- (h) Snap and Systems Audit Report;
- (i) any special inspection/investigation report; and
- (j) Computer/EDP Systems Audit.

2. Circulars in connection with Accounts/financial statements:

Please confirm that you would be in a position to make available, for our ready reference, a list and copy (preferably in a separate folder), of all the HO/CO/RBI circulars, relevant to the accounts for the year 2007-08. **A copy of the year-end Closing of Accounts Circular(s), also needs to be given to us.**

3. Accounting Policies:

We understand that there is no change, since the preceding year, in the Bank's Accounting Policies adopted and applicable for the year under audit.

Should there be a change as compared to the earlier year, we may be duly informed of the same and the financial effect thereof may be computed to enable us to verify the same.

4. Balancing of books:

Please confirm the present status of balancing of the subsidiary records with the relevant control accounts.

In case of differences between balances in the control and subsidiary records, please let us know of the steps being taken to reconcile/balance the same.

This information may please be given head-wise for the relevant control accounts, indicating the dates of arrears of balancing.

The year-end status of balancing may be reconfirmed.

Any balancing differences reconciled after the year-end may please be brought to our notice in the course of audit.

5. Accounts, if maintained on Computer/ in the EDP environment:

- (a) In case the financial information/data is being prepared in an EDP environment at the Branch, please confirm:

- (i) whether, **and the extent to which:**
- the Branch records are not yet computerised, and
 - outstanding balances picked up at the time of initial computerisation, remain unadjusted/ unreconciled. **Head-wise figures taken over from the manual system, and included in the balances as at the beginning of the year and which continue till date may be confirmed, with status of their analysis/ adjustment during the year.**
- ii) the kind/nature of **software package(s) currently installed** at the Branch; and whether there are any changes/ modifications in the package(s) since the preceding year both as regards the systems as well as changes brought about by virtue of regulatory/statutory amendments and H.O. Circulars, including due to applicability of revised interest rates on deposits, advances etc.

The nature of such modifications, the basis thereof and the effective dates of the modifications , may please be confirmed to us.

- (iii) **Please let us have a confirmation that the print-out of books is taken and is available for our examination, simultaneously with the branch returns/statements i.e. on 1.4.2008;** unless otherwise stated in our letter, or where some matters can be explained/ dealt with prior to the year-end.
- (b) Please confirm the precise procedures for computer security systems and data security, back-ups, off-site storage (including locations and personnel in charge), contingency and disaster recovery system/plans and adherence thereto at the Branch.
- Off site storage locations may be indicated along with information as to the periodicity of testing the data, and whether such periodicity was adhered to.
- Any adverse features observed during the year may be confirmed, along with the remedial action taken.**
- (c) Please keep ready for our examination, the **daily exception reports** on the “system” as well as “**transactions**”, to enable us to examine the manner of disposal of the reports generated; as also the report for the month-end/day-end procedures as at the year-end.

6. Deposits

(a) Overdue/matured Term Deposits:

- (i) We understand that as per your H.O. circulars and in keeping with the circulars of the RBI, you have introduced a system for automatic/suo moto renewal of term deposits on maturity.
- The cut-off date(s) beyond which these instructions apply may be intimated to us, indicating as to the status and basis of interest accretion, if any, on the amounts held as Overdue Deposits in the Accounts of the Branch.
- Please confirm whether there are any credit balances comprising overdue/ matured Term Deposits in various categories, as at the year-end, which continue to be shown as Term Deposits, particularly where the Branch does not have any instructions/ communication for renewal of such deposits from the account holders.
- (ii) In case of automatic renewal of old matured deposits in terms of your H.O. circulars, please confirm as to the basis adopted at the Branch for computation of the interest component (added to the original principal), for purpose of renewal, i.e. whether it is on:
- simple interest since maturity of the original/initial deposit; or
 - based on interest rate applicable on the date of maturity of the deposit; or
 - based on the rate of interest on the date of renewal of the deposit.

and whether any excess/short provision relating to the prior periods i.e. up to 31.3.2008 is considered in the accounts under review.

The computation of interest may be evidenced for our verification.

The number and amount of such deposits may be confirmed, *both for Rupee denominated as well as for foreign currency deposits.*

(iii) Please let us have a list of deposits, which have been received/ suo moto renewed but where:

- deposit receipts are not physically issued, although book entries have been made as per the computerized system,
- deposit receipts are physically issued but not dispatched to deposit holders (particularly where the amounts received in foreign currency are to be covered by Deposit Receipts from another foreign exchange authorized Link Branch.

A list of such unissued/undispatched Deposit Receipts in the physical custody of the Branch needs to be given and the Receipts produced for our verification at the year end.

- renewals have been made by endorsement of renewal on the existing Deposit Receipts of the deposit holders.

This may be substantiated from your record.

For the above, information may be prepared for deposits:

- in Rupees
- held in foreign currencies - FCNR(B) Deposits
- in external accounts (NRE accounts, if any).

(iv) Please also confirm whether any deposits have been renewed other than in the name(s) of the original holder e.g. in the case of deceased depositors.

In such cases, it may be confirmed to us as to whether the Branch holds the necessary evidence on record.

(b) **Tax Deduction at Source**

Please confirm the system followed by the Bank with regard to deduction of tax at source on interest on deposits and whether:

- in respect of interest (**based on credit or payment whichever is earlier**), including in respect of cumulative Deposit Schemes and on renewals of matured deposits, Tax as required to be deducted at source was so deducted on due dates and deposited within the prescribed period; and
- the automatically renewed deposits are net of the Tax deducted at source.

Cases of delay/default may be listed for our review and incorporated in Form 3CD (Tax Audit Reporting Format).

(c) **Back-ended or other subsidies adjustable against advances**

Please confirm whether Deposits include any amounts received under specific schemes. If so, the amount thereof and interest, if any, paid thereon during the year, may be confirmed; and whether interest on advances is calculated net of Govt. subsidies in such schemes.

(d) **Deposits held as margins:**

Please confirm whether against issue of guarantees/ LCs, the Branch holds any cash margins by way of fixed deposits, shown as part of the 'Deposits' portfolio.

If so, the aggregate amount of such deposits may be made known to us.

(e) **Inoperative Deposit Accounts:**

Please confirm the procedure followed at the Branch with regard to identification of Inoperative Accounts and safeguards as to operations therein; **and whether the identified accounts are segregated/maintained in separate distinct ledgers.**

Please let us have information as regards:

Aggregate Opening Balance

Additions/Accounts identified during the year

Less: Payments out of such accounts

Balance Outstanding at the year end

7. **Advances:**

- (a) Please confirm whether the aggregate of the advances as per the Branch Balance Sheet as at 31.3.2008 reconciles with the Particulars of Advances (Portfolio) statement after including credit card dues and making adjustments for any foreign exchange differences (if on a decentralized basis); as well as after considering the unadjusted / unappropriated credit balances (**whether in specific or nominal accounts**) and requiring adjustments/netting off against the borrowers' accounts **which would include accounts like "Interest Suspense", DICGC claims Received" and unappropriated recoveries in Advances in litigation and subsidies (and interest thereon, to the extent requiring adjustment).**

A summary of the particulars of Advances as per Annexure II may be provided to us.

- (b) A list of all Advances, each with outstandings above 5% of the total Advances Portfolio of the Branch or Rs. 200 lakhs whichever is lower, indicating their classification.

The year-end Status Report on each large borrower, may be given as per Annexure III, III.1 and III.2, which includes information as per the LFAR.

The aforesaid information, (which must also cover accounts adversely commented upon by Bank's internal/ concurrent auditors/ RBI inspection/ special audit/ credit audit/ previous statutory auditors- i.e. in the Reports as per refer Para I of this Annexure), may please be prepared keeping in view the applicable RBI circulars, and kept ready and be made available to us along with the Branch returns on 1.4.2008.

- (c) **Besides providing us information as per Annexure II, may we request you to provide us with a list of the:**

- (i) Top 25 NPAs and their status as at 31.3.2007 and 31.3.2008;
- (ii) Borrowers identified/classified as NPAs during the period 1.4.2007 to 31.3.2008 and whether and extent to which unrealized income on such accounts is reversed/derecognized;
- (iii) NPAs upgraded to Standard classification during the period 1.4.2007 to 31.3.2008, justifying reasons for the same; **also indicating the amount of any unapplied interest in such accounts (not debited/charged to the borrower);**
- (iv) Accounts where there was rehabilitation/reschedulement/restructuring, indicating in each case, **the number of times the same has been done**, and accounts in which the Bank needs to exercise its **right to recompense**, indicating the amount, also giving reasons for non-recovery thereof;

{The aggregate of such amounts due (*party-wise*), and the dates on which recoupment is to be made, may please be made known}.

- (v) Cases covered by restructuring of advances, where borrowers were granted FITL facilities or where the interest unrealized was converted to investments by the Bank.

BANK BRANCH AUDIT (2007-2008)

- (vi) Cases of rehabilitated/restructured borrowal accounts at the Branch, where the classification is not as per RBI norms; or where any amount of sacrifice is not computed/provided.

Information on accounts restructured may be provided as per Annexure IV.

- (vii) List of Borrowers, where one time settlement was sanctioned, but there is a default in repayment or in compliance of the terms thereof;
- (viii) Particulars of Advances where there is divergence of opinion between the Branch Management and the RBI/Inspection/ Internal/Concurrent audit Reports etc., indicating as to how this has been addressed by the Branch.
- (ix) The aggregate of the amounts of advances in the standard category which have the status of "critical amount due"; and whether any amounts comprised therein are over 90 days in default as at 31.3.2008.

A list of such accounts may be made available and quantified, for our review.

- (x) Borrowal accounts (in standard category), which have not been reviewed/ renewed for 180 days since the due date of their last renewal, or where there is a default on the part of the borrower in submission of stock statements, for a period of 90 days beyond any period of default/irregularity, **including that commencing prior to 31.3.2007**; and if so, whether such borrowers are classified as NPAs.

Particulars of accounts overdue for review/renewal between 6 months and 1 year, and those over 1 year may be provided.

- (xi) accounts which do not fall within the definition of advances, such as interest free employee advances, but have been shown as such in the accounts of the Branch may be listed for our review.
- (xii) advances accounts which have been identified as of the nature of NPAs, and where, pending formal sanction of the higher authorities, the relevant amounts have yet to be reclassified/recategorised for the purpose of provision/write off. **This covers all accounts identified by the Bank or internal/external auditors or by RBI inspectors but the amount has not been written off wholly or partly.**
- (xiii) accounts in which the Bank, or the Branch has itself recommended legal or other coercive action for recovery of dues and, where no such action has been taken up to the year -end against the borrowers. A list of such borrowers' accounts may be furnished to us, particularly if such accounts are in standard or sub standard category.
- (xiv) borrowal accounts in the "Standard" or "Sub Standard" category which are the subject matter of reference to BIFR/ DRT or in litigation.
- (xv) Advances to borrowers on the list of willful defaulters (as per the latest list and guidelines of the RBI).
- (xvi) all accounts where the default resulted in WCTL, FITL, WCDL etc. and whether the advances would be NPAs but for such facilities.
- (d) **Please confirm whether:**
- the borrowers' accounts have been classified according to the latest RBI norms applicable for the year, with particular care being taken to identify Non-Performing Assets(NPA) [**classified as Sub-Standard, Doubtful or Loss assets**], and, in case a computerized package is being used for such an exercise, **whether the statements are being prepared with the applicable latest parameters as per the prudential norms of the Reserve Bank of India (Refer also Section E, E.I, E.II and E.III);**
 - you have examined the accounts based on documentation security/guarantee/ operations aspects etc. to determine the status **borrower-wise** and not account-wise

- for categorising the accounts, as above;
- the classification as at the year-end of borrowal accounts under consortium arrangements with other participating banks, has been done on the basis of operations of the accounts as per your Bank, without the necessity of relying on classification made by other participating banks; **however, making known to us, the status of the borrower, if adverse, in case of other lenders.**
- the Borrower's classification at the Branch is uniform for the Bank as a whole, based on the applicable RBI norms, in case of sub-limits/ transferred limits and where advances are transferred from another branch.

(e) **Valuation/market value of tangible Assets:**

Please confirm:

- whether in respect of the advances secured against tangible securities, the bank holds evidence **of existence and market value** of the relevant securities as at the year-end.
- whether the existence/market value is evidenced, based on physical inspections or otherwise through stock audit or other verification procedures applied nearer the balance sheet date; and the same may be produced for our examination.
- in case of NPAs, the periodicity of valuation, and the basis on which valuation is arrived at in respect of advances for the year under audit, particularly in case the security valuation reports/dates are older than one year.
- in respect of facilities of Rs.5.00 crores and above, whether stock audit has been got conducted.
- whether and in which cases was the stock audit was required to be conducted. Please furnish us:
 - > **List of accounts where stock audit was required, but not conducted; and**
 - > **Cases in which stock audit was conducted where adverse features noticed have not been addressed and whether it has any effect on classification of any borrowers; and whether the same has been duly considered.**

(f) **Upgradation of classification:**

Please let us have a list of borrowers' accounts (including projects under implementation and restructured accounts), where classification made as at the end of the previous year (31-3-2008), has been changed to a better classification, stating reasons for the same; and whether provision (including for the Interest sacrifice, if made), on the borrowal accounts, is sought to be reversed contrary to RBI's master circular.

Please confirm whether Advances comprising Funded Interest, if already recognized as income, is fully provided for and not reckoned as income till realization/ redemption of securities.(This would also apply to funded interest where the same is converted into securities (equity, debentures or other instruments), if held at the branch.

(g) **Devolved Letters of Credit(LCs)/ co-acceptances, and guarantees:**

Please confirm:

- the precise procedure followed for accounting treatment of devolved, LCs.
- whether in categorising the borrowers' accounts as standard, substandard, doubtful or loss assets, the amount in default on account of devolved LCs has been reckoned, as per the applicable RBI norms.
- whether there are any devolved LCs upto the year-end.

Please also confirm whether the debits have been raised in separate distinct accounts of the borrowers or to the normal cash credit/overdraft accounts of the borrowers; and if not, whether these are considered for classification of the borrower.

For Information on guarantees invoked, and outstanding LCs/ co-acceptances. Refer format in Para 5(e) of Part 1 of the LFAR questionnaire.

(h) Please confirm:

- (i) Whether in computing the Drawing Power(DP), Sundry Creditors comprising unpaid for stocks, are reduced prior to application of margin as stipulated.

A list of cases where such reduction was not specifically made(**including by the leader bank in consortium**), may be made known and particularly where it has an adverse effect on the borrowers' status. Please review all cases of the stock confirmations/certificates issued by the borrowers to the Bank to determine if, and to the extent, the DP is required to be modified on this account and as may have a bearing on the limits/drawing power. This may also be evidenced for us.

- (ii) In case of one time settlement proposals under consideration or where rehabilitation/ rephasing is being done, whether the amount of sacrifice including anticipated sacrifice is provided fully.

Particulars of accounts where the borrowers have defaulted in their commitments after sanction of the compromise proposal, indicating classification of the amounts, may be made available to us.

The extent of provision/ adjustment, if any, made may be communicated.

- (iii) Whether the Bank has a recovery policy in cases of compromise/ settlement/ write off and is the policy available at the Branch.

Particulars of cases of compromise/settlement/write off involving write off/waiver, each in excess of Rs. 25 lacs, may please be furnished.

- (iv) the particulars of any borrowal accounts with working capital limits of Rs.10.00 lacs and above, as also in case where audit is compulsorily required as per any statute, where the latest audited accounts are not on record.

- (v) Compliance by the Branch of the RBI Master Circular, relating to statutory and other restrictions as regards Loans and Advances.

In particular it may be confirmed as to whether:

- there are any loans and advances against security of the Bank's own shares.
- there is any laid down procedure as regards identification of directors/ officers and their relatives **and** of directors of other banks for purposes of sanction of loans to them or to concerns in which directors are interested, as per the said circular.
- loans have been given to companies for buy back of their shares/securities.

(i) Advances to share brokers/NBFCs:

Please confirm whether at the Branch, there are advances to:

- share brokers; if so, the total amount of limits granted and the aggregate advance due as at the year-end.
- NBFCs; if so please confirm whether the Reserve Bank of India has taken any adverse view as regards their registration or otherwise.

The status on advances to NBFCs may please be made known, along with their classification.

(j) Advances to Staff

Please confirm:

- the procedure with regard to Advances to Staff (interest/non-interest bearing), by the Bank, both in its capacity as a banker and as an employer; also whether such interest-bearing advances are being disclosed as Advances.
- the verification procedures followed in respect of Staff Housing Loans, and in particular, whether the original documents are held at the Branch and can be produced for our examination.

(k) Credit Cards :

Please confirm the system followed at the Bank/Branch for recovery of credit card dues; and whether, and the extent to which, there are:

- any debits in the Branch on account of credit card facilities, and whether the amount is being reflected as part of the ADVANCES portfolio or as part of OTHER ASSETS;
- any arrears/ defaults in collection of such dues; **and**
- unadjusted debits up to the year end, against the Credit Card holders' Current/ Savings Accounts.

8. Outstandings in Suspense/Sundries:

Please let us have a summary of the year-wise break up of amounts:

- debited to Suspense Account (or similar account) indicating the number of entries and the amount thereof, with reasons for non-adjustment of old/large/unusual entries. **The amount of provision for doubtful debits may be confirmed.**
- credited to Sundries/Sundry Deposit Accounts, indicating the reasons for non-adjustment of items included therein, particularly in respect of items which are over 3 years old.

(Information may please be provided in the formats as per the revised LFAR).

9. Provisions/Liabilities remaining unadjusted against corresponding advances:

Please confirm whether:

- provisions for known liabilities, including for Fringe Benefits Tax, up to the year end have been made (also, based on subsequent entries made); and
- there are any advances (e.g. Travel Advance) against such provisions/liabilities that require to be netted off for purpose of the financial statements.

If so, the same may be made known to us, to the extent unadjusted at the Branch.

10. Inter-branch/Office Accounts/Head Office Account:

- (a) Please let us have a statement of entries (head-wise) which originated prior to the year-end at other branches, but were responded after the year-end at the Branch.

This statement may please be prepared upto a cut off date if stipulated by Head Office, and if not, upto the date of completion of audit but before submission of our report. (Format at Annexure VI may please be used and handed over).

- (b) Date-wise details of debits in various nominal or other sub-heads relating to Inter-branch transactions, with reasons, particularly for large outstanding amounts, including those which are pending for over 30 days as at the Balance Sheet date.

- (c) **Please confirm:**

- **whether, and the extent to which, there are (under any sub-head), any debits outstanding over 6 months as at the year-end**, and whether provisions are being considered against the same at the Branch level;
- whether the Branch has effectively complied with the centralised Reconciliation Cell, all their queries in relation to unmatched entries.

Communications as are pending action, may be made available for our review.

- the number of old unadjusted entries and the aggregate amount as at the year-end comprising unlinked debits in respect of Drafts and TTs, MTs paid, which remain outstanding at the Branch; and whether, and the extent to which, provision is being considered for the same.
- (d) Please confirm the period upto which the Reconciliation Cell has sent the statements of unmatched entries (head-wise).

11. Foreign Currency outstanding transactions:

If the system of conversion of foreign exchange entries has been decentralized, the precise year end adjustments made in the Branch Accounts (**head-wise**) may please be made known to us.

Please confirm whether all balances (including off-balance sheet items) outstanding in foreign currencies as at the year-end have been converted as at the year-end rates as applicable; or at the rate(s) as at the date(s) of origination thereof.

Evidence/basis of the rates as applied may be made available.

12. Contingent Liabilities etc.:

Please confirm whether:

- other than for advances, there are any matters involving the Branch in any claims (both statutory, contractual or otherwise) in litigation, arbitration or other disputes in which there may be some financial implications, including claims from customers, fraud cases, for staff claims, municipal taxes, local levies etc. If so, these may be listed and evidenced for our verification, and you may confirm whether you have included these as contingent liabilities in the Branch financial statements.

(Reference may also be made to the LFAR - Para II.3).

- guarantees are being disclosed in the Branch Balance Sheet, **net of cash margins and term deposits**, or otherwise; and whether, and the extent to which, expired letters of credit, and guarantees **where the claim period has also expired**, continue to be disclosed in the Branch returns.

The amount of such expired obligations may be made known.

- there are any other obligations assumed, eg. **Letters of comfort**; of so, whether the amount of such obligations is being disclosed in the Branch financial statements.
- there are any outstanding contracts on capital account (including for fixed assets to be acquired/constructed). Details thereof may be given.
- there are any awards in arbitration/litigation or disputes involving any liability (including based on any awards by the Banking Ombudsman)

13. Interest Income/Expenditure:

- (a) Please let us have a statement showing the rates of interest applicable during the year on various
- Advances Accounts
 - Deposits Accounts

giving reference of the relevant circulars of the Head Office, and indicating the effective dates and periodicity of application of the interest rates; and evidencing that the computer programme was modified from such effective date(s).

This information may be sent now, and changes hereafter may be communicated later as and when these take place.

Please confirm whether interest being debited at the end of each month on advances, is also being compounded for levy of further interest on a monthly basis. Rectification, in respect of interest if not properly charged up to the date of modification of the interest rates during the year, may please be advised to us, along with the changes/modifications, if carried out in the software programme.

Please confirm whether the changes are reflected in the contracted rates as per documentation.

(b) System of appropriation of recoveries in NPAs:

Please confirm the basis on which recoveries in NPA Accounts are being appropriated, in particular where recoveries are in excess of "Interest Suspense" – **whether priority is being given towards principal or unapplied interest.**

Please confirm whether there is any amount of "Interest Suspense" or "Unapplied Interest" or a "right of recompense" in borrowal accounts classified as "Standard".

If so, details thereof may please be given to us.

(c) As regards advances (including bills), whether:

- any income has been adjusted/recorded to revenue, contrary to the norms of income recognition issued by the Reserve Bank of India and/or Head Office circulars issued in this regard; and particularly where the chances of recovery/realisability of the income are remote.
- in respect of accounts classified as NPA during the year, including as at 31.3.2008, the income remaining to be realized(i.e. unrealized) for the preceding year is reversed to income or provided for; and that for the year 2007-08 such unrealized income is derecognised.
- any income has been recorded on Non Performing Accounts (including overdue bills) other than on actual **realisation** from the borrowers, or out of fresh limits sanctioned by the Bank.
- the reversal of interest income (i.e derecognised income), is recorded through «Interest Suspense» or similar account.
- unapplied interest has been computed and recorded upto date.

(Please confirm whether the contractual or any other interest rates are the basis of computation of unapplied interest).

- Unrealized fees, commission and other charges in respect of accounts identified as NPAs during the year, are reversed for all earlier periods.

Amount of income accrued, if any, as at 31.3.2008 on NPAs may be made known.

- whether interest adjustments on inter branch balances as communicated by Head Office, have been duly recorded in the Profit & Loss Account.

Relevant evidence thereof may please be made available to us.

14. Commission on Govt. business

Please confirm whether at the Branch, income is being accounted on cash basis or on accrual basis. Income accrued upto 31.3.2008 but not claimed/ recorded/ received may please be confirmed to us, together with computation thereof.

Income Receivable by the Branch based on business done upto 31.3.2008 may be got computed and made known, if the same is required to be recorded at the Branch level.

15. Interest Provision:

Please confirm:

- (a) whether interest provision has been made on deposits etc. in accordance with the latest instructions of the Head Office.

A copy of these instructions may be made available for our information. the amount of interest accrued and due but not applied (since the date of last application) on Savings Bank Account deposits; and further let have the basis of such computation for each code head.

- (b) Whether interest accrued and due on Deposits only forms part of the deposits portfolio (under the respective subheads) and that interest accrued and not due is reflected as part of OTHER LIABILITIES.

16. Employee/Staff Payments and benefits

Please confirm that all payments due to the Branch employees upto the year end, have been duly computed and recorded under the respective sub heads, including incremental liability towards arrears, if any.

17. Rent, Rates and Taxes

Please confirm that the rents, rates and taxes are recorded up to the year end, based on:

- rent/lease agreements for the time being in force and liability has been considered on the basis of claims/demands and contractual enhancements due;
- municipal taxes and levies are adjusted/provided up to the year-end, based on the demands accepted; and
- in case of disputed liabilities, if any, the related contingent liability has been disclosed.

18. Penalties/fines etc:

Please confirm whether any fines or penalties have been imposed on the Branch, or incurred or paid by the Branch during the year as arising out of any defaults to meet statutory or regulatory requirements or otherwise. If so, the particulars thereof may be made known; as these would require separate disclosure in the financial statements of the Bank and for consideration in the Tax Audit Report under Section 44 AB of the Income tax Act 1961 (Form 3 CD).

19. Balance(s) with other Banks(including RBI/SBI):

Please confirm the status of reconciliation as at 31.3.2008, of accounts with other banks in your Branch; as also whether there are any entries arising therefrom as have effect on revenue up to 31.3.2008, which remain to be adjusted till the year end. For this purpose you may let us know how the pending items in reconciliation were adjusted after 31.3.2008, and whether these are considered in the Memorandum of Changes (MOCs).

20. Frauds etc.:

Please confirm whether for the purpose of provisioning, the relevant particulars have been prepared at the Branch and whether:

- there are any frauds reported/recorded upto 31.3.2008;
- the Branch has complied with the reporting requirements of RBI and communicated the same as per the requisite formats.

- there are any cases of vigilance or similar enquiry, or financial claims from customers/ others in respect of the Branch. The relevant records of these may please be made available.
- any enquiries have been initiated for any suspected frauds/aberrations.

If so, particulars thereof may be furnished.

Recommendations of the Mitra Committee – Bank Frauds

While drawing your attention to the contents of the AAS 4 issued by the Institute of Chartered Accountants of India, particularly in that the responsibility for the prevention and detection of fraud and error rests with the management through the implementation and continued operation of an adequate system of internal control, we would request you to confirm whether, in relation to the operations/activities of the Branch, anything has come to light which is in the nature of a fraud, any fraudulent activity, or any matter susceptible to fraud or foul play, which should receive our attention; and particularly, if there is anything which invokes, or is the subject matter of any vigilance, enquiry, investigation or examination as regards any transaction or event that is suggestive of attracting compliance or for reporting to the competent authorities within the Bank, or to the regulatory authorities.

This would include matters that could arise out of inadequacies in, or absence/breach of the laid down internal control systems and procedures (both accounting and administrative).

21. Asset Liability Management:

Please let us have, duly authenticated, the financial information regarding the additional disclosures to be made as at 31.3.2008, as required by the Reserve Bank of India, indicating the procedure followed to arrive at the financial data.

Instructions from the Controlling Authority, in this behalf, may be made known.

22. Long Form Audit Report-Branch response to the Questionnaire:

In connection with the Long Form Audit Report, please let us have complete information, and evidence, as regards each item in the questionnaire, to enable us to verify the same for the purpose of our audit.

Reference may also be made to the important items as per **Annexure VII**.

23. Tax Audit in terms of section 44AB of the Income-Tax Act,1961:

Please let us have the information required for Tax Audit under section 44AB of the Income-tax Act, 1961 to enable us to verify the same for the purpose of our report thereon.

24. Compliance of Ghosh and Jilani Committee recommendations

Please confirm whether the Branch has duly complied with the requirements of the Ghosh and Jilani Committees and whether such compliance has been got verified from the Bank's Inspection Division and/or the Concurrent Auditors.

It may be confirmed as to whether there are any adverse observations in respect of any requirements; and if so, these may please be made known to us.

25. Consideration of laws and regulations for the purpose of the audit of financial statements:

Please confirm as to whether the Branch is maintaining a codified list of the related laws and regulations applicable to the Bank in respect of its operations/activities to cover all transactions and events, with which it is concerned; and whether the Branch management has come across, or is aware of anything that needs to be brought to our notice for our consideration or anything suggesting that there is fundamental effect on the branch state of affairs or operations on account of non-compliance of these.

26. Other Certification

Please let us have, duly authenticated, information as regards other matters which, as per the letter of appointment, require certification/validation.

The certificates relate to the following (besides the data as the letter of appointment, and assistance may be sought from the Annexures indicated):

- (a) DICGC
- (b) PMRY
- (c) 12 odd dates data for verification of SLR (Refer Annexure VIII)
- (d) Additional Disclosures
- (e) Implementation of the Ghosh and Jilani Committee recommendations
- (f) Movement Chart of NPAs and Provision of NPAs (Refer Annexure II)
- (g) Information relating to restructuring etc. undertaken during the year

Please confirm whether the Branch maintains the prescribed records relating to the cash withdrawals beyond the prescribed limits and whether tax has been collected and remitted to the authorities within the prescribed time.

27. Transactions and events after the Balance sheet date

Please let us have a statement of any significant transactions or events accruing after the Balance sheet date but which relate to the period prior to 31-3-2008, **whether or not yet recognized or recorded in the accounts of the Branch**. This would include items of income or expense or capitalization etc. relating to the period prior to the year end .(particularly also, these are reported in the inspection/internal/concurrent audit reports relating up to March 2008), which need to be incorporated in the MOC. This may kindly be communicated to us.

28. Investments:

In case the Branch holds any investments on behalf of the Bank:

- (a) these may be produced for physical verification and/or evidence of holding the same be made available.
- (b) stock of unused security paper stationery/numbered forms like B/Rs, SGL Forms etc. may please be produced for physical verification.
- (c) it may be confirmed whether income accrued/collected has been accounted as per the laid down procedure, and is not reckoned as income of the Branch.

The procedure may please be confirmed to us.

Information duly completed in respect of Paras 21 to 28 should be made available simultaneously with the returns/ statements/ schedules, as committed by the Head Office to be given by the Branch on 1.4.2008.

CHARTERED ACCOUNTANTS

BANK BRANCH AUDIT (2007-2008)

ANNEXURE - II

Information on Advances

I. CLASSIFICATION OF ADVANCES AS COMPARED TO THE PREVIOUS YEAR-END (Amt- Rs. In '000)

Particulars	As at 31.3.2008		As at 31.3.2007		Increase/ (Decrease)	Provision	
	No.	Amt (Rs)	No.	Amt.(Rs.)		Amt(Rs.)	2008
A. STANDARD							
a) SME/Dir. Agriculture							
- residential housing loans beyond Rs.20 lacs							
-personal loans(including credit cad receivables), capital market exposures, commercial real estate loans and to Systemically Important non deposit taking NBFCs							
-Others							
Total (A)							
B.SUB-STANDARD							
C.DOUBTFUL							
D.LOSS							
E.Total(B+C+D)							
TOTAL (A+E)							

II. PARTICULARS OF AND MOVEMENT IN NPAs AND PROVISIONS

	<u>GrossNPA(Rs.)</u>	<u>NetNPA(Rs.)</u>	<u>Provision(Rs.)</u>
As at the beginning of the year			
Additions during the year			
Less: <u>Deductions</u>			
a) Recoveries			
b) Write Off			
c) UpgradationWrite back			
d) Others (Specify)			
	-----	-----	-----
Balance at the year-end			
	=====	=====	=====

BANK BRANCH AUDIT (2007-2008)

III Interest etc. (ACCRUED BUT NOT EARNED) on NPAs

	31.3.2008		31.3.2007	
	No. of Accounts	Amount (Rs.)	No. of Accounts	Amount (Rs.)
Interest Suspense				
Unapplied Interest				
Right of Recompense				
TOTAL				

IV . LOANS SUBJECTED TO
RESTRUCTURING/REHABILITATION/RESCHEDULEMENT/RENEGOTIATION

Category	2007-2008				2007-2008			
	No. of Accounts		Amount(Rs.)		No. of Accounts		Amount(Rs.)	
	CDR	Others	CDR	Others	CDR	Others	CDR	Others
Standard @*	-----	-----	-----	-----	-----	-----	-----	-----
Sub –Standard*	=====	=====	=====	=====	=====	=====	=====	=====
Doubtful *	=====	=====	=====	=====	=====	=====	=====	=====
Amount of sacrifice								
@ FITL Component included								
Trading facilities if included above								
	=====	=====	=====	=====	=====	=====	=====	=====

[*restructuring under CDR to be separately stated for each category]