

BANK BRANCH AUDIT – PLANNING AND DOCUMENTATION

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INTRODUCTION & IMPORTANCE:

- The Banking sector has seen a sea change over the past twenty five odd years gradually shifting from a totally regulated environment to a totally market driven competitive system and just regulator driven at a macro level.
- High quality of audits complementing supervisory efforts of the regulators in risk management only can ensure safe and sound banking systems.
- The industry has seen a plethora of sweeping changes in the areas of prudential and IRAC norms and in the regulatory norms. These changes coupled with commendable technological upgradation in the operations of banking have considerably widened the scope of the Statutory Audit of Banks. In other words Statutory Audit is not a mere certification of the year-end figures of the Final Accounts but it entails quite a number of certification after due verification of lot of facts and figures thereby rendering the audit of Banks highly risky unless the nuances of banking are fully understood and tackled properly through proper planning and execution.
- The banking industry like any other industry has its own ups and downs and this is one industry which suffers when the economy is not performing well and is sluggish. The year 2015-16 was a not so good year for the industry in general and several banks had sustained reported very huge losses of unimaginable magnitude.

Changes during 2015-16 :

Asset quality review by RBI

Special dispensation given for restructuring of advances has been predominantly done away with

Guidance note on audit of banks (2017 edition) should be gone through and it provides exhaustive guidance on every aspect - acceptance, planning, performance and documentation of the audit.

ICAI also operates a help desk for providing guidance to members for specific practical issues concerning bank audit.

PLANNING AND DOCUMENTATION

Planning - Importance:

By failing to plan, we plan to fail

“Enni thuniga karumam thuninthapin

ennuvam enbathu izhukku.”

“Think wisely (plan) before you exercise an action. Having done so however, never look back and regret. That would be a shame”

Getting prepared – Pre commencement:

Give me six hours to chop down a tree and I will spend the first four hours sharpening my axe.

As auditors we need to equip ourselves with updated knowledge on banking industry particularly in the light of frequent issue of circulars by the regulator and that too at the fag end of the year or at times in mid April too. At the same time the auditors should have a thorough knowledge of the latest Auditing Pronouncements issued by the ICAI so as to enable them to discharge their responsibilities efficiently and also to uphold the trust reposed in us by the various sectors of the economy. In a nutshell, a unique approach, in the form of highest professional competence and skilled manpower, is necessary to carry out the audit of banks effectively given the hectic constraint of time.

Documentation helps in making an “experienced” auditor appreciate that an effective audit has in fact been conducted by reviewing the audit evidences for the basis of the audit report / opinions and that audit has been planned and performed in accordance with SAs on auditing and applicable legal and regulatory requirements.

The link between planning and documentation –

While planning makes audit effective and efficient, documentation helps in making a reviewer appreciate that in fact an effective, efficient and proper audit was carried out.

SA 230 – Audit documentation

When should documentation be done:

Though standards on auditing consider around 60 days from the completion of audit to be reasonable to put in place the audit documentation (final assembly file), it would be only imperative to document on the go. Documentation process would start with the receipt of an appointment letter and would end with the issue of audit reports and other certificates.

APPROACH:

- Banks start contacting the auditors for their consent to be the auditors for their proximal branches. For some of the auditors it will be a difficult decision to make a choice if more than one bank approaches them. However two aspects have to be kept in mind before conveying one’s consent:
 - A. Indebtedness to the bank – 2004 circular i.e. no credit facility should be availed (including guaranteeing any facilities availed by a third party) of by the proprietor / any of the partners of the audit firm / members of his / or their families or by firm / company in which he / they are partners / directors (Independent directors).

- B. The auditors should not undertake statutory audit assignment if they are associated with internal assignments in the Bank during the same year. If it is so, they should relinquish the internal assignment before accepting the statutory audit assignment during the year.

Key deliverables in a bank branch audit:

- Audit report – Whether requirements of SAs met
SA700 - “Forming an Opinion and Reporting on Financial Statements”
SA 705 -“Modifications to the Opinion in the Independent Auditor’s Report”
SA 706 -“Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor’s Report”
- Authentication of closing returns including those containing details relating to disclosures – NPAs, provisioning, movement, restructuring, etc.
- Long form audit report (LFAR).
- Tax audit report
- Authentication of data relating to computation of capital adequacy ratio
- Certificate in respect of DICGC claims
- Report on status of the compliance by the bank with regard to the implementation of recommendations of the Ghosh Committee relating to frauds and malpractices and of the recommendations of Jilani Committee on internal control and inspection/credit system.
- Certification on claim of various subsidies and interest subvention
- Knowledge about the activities and operations of the branch – service, advance oriented, deposit oriented, would help in attaching due importance for each of the above deliverables.

TIME FRAME AND REQUISITES

- In audit of Banks in general, be it central or branch the time frame within which the audit is to be completed is of utmost importance.

The following shall be useful in planning the Audit:

- Particulars and location of branches including the means of transport to reach them
- Particulars of central auditors under whose purview the branch falls.
- Particulars of previous auditors – Communication with the previous auditors through RPAD or any mode with a positive confirmation of delivery. If communicated through mail, it is always advisable to subsequently procure the hard copies of the letters and proof of delivery and file the same in the audit files.
- Procedural requirements regarding acceptance
- Besides the main report and LFAR, the various certificates to be given
- Computation of audit fees and scales of allowances and conveyance expenses.
- Nature of Branch operations – Deposit oriented or advance oriented – overseas – Retail – Industrial or Agricultural – Service branches – Government transactions.

- Letter in advance to the branch listing the auditor's requirements and materials necessary for the purpose of audit to be kept ready by the branch at the time of his visit. The following aspects are to be covered in the letter depending upon the nature of the branch:
 - Copy of the HO circulars / instructions issued for the year
 - List of Accounting policies followed notifying any changes during the year as compared to the previous year. This may need a special attention during planning and execution
 - Copies of the various audit reports of the branch.
 - Confirmation as to reconciliation / balancing of books.
 - Certificates regarding cash balance, bank balance u/s 269T and 40A(3) of IT Act, 1961 contingent liabilities etc.
 - Confirmation as to interest provision on deposits and advances as per HO instructions.
 - Returns relating to advances and their classification with ultimate summary – Sector wise, security wise and Prudential norms.
 - Up gradation, down gradation and new NPAs along with interest reversal.
 - Restructured advances and related provisions.
 - Movement of NPAs.
 - LFAR requirements – Besides advances, BGs details, outstanding sundry assets / suspense, Bills payable and sundry deposits, inter branch accounts, details of frauds, if any and note regarding extent of computerisation, internal control access and data security measures, details of matured deposits and details of joint custody of cash.
 - Tax audit u/s 44AB requirements – Depreciation schedule if any, list of books maintained, taxes duties etc u/s 43B, TDS details along with challans and returns filed, prior period items.
 - Certificates – capital adequacy, maturity pattern of loans and deposits – Various subsidies, interest subvention, KYC etc.
- Master circulars and other circulars issued during the year, Master Guidelines issued during the year.
- Any significant happening during the year that may have an impact - Demonetisation

COORDINATION WITH THE CENTRAL STATUTORY AUDITORS

- Annual closing circular though is a main mode of communication between HO and its sub-ordinate offices including branches, it is also an important document of communication by the SCAs with the SBAs as this circular is normally vetted by the SCAs to exhaustively include their expectations.

- Some banks organise a meeting between the branch auditors and the central auditors so as to have an interaction with each other to share and know the experiences and expectations as well as clarifications on issues may be sought for in the presence of ZO / RO executives. This type of meeting enables the auditors to define and understand their roles and responsibilities in clear terms which may lead to an effective audit. Some of the banks hold such meetings as a matter of formality rendering little at the final outcome of the meet. Some of the banks do not hold such meeting citing it as an expensive affair unmindful of its benefits. On the other hand, some of the branch auditors do not attend these meetings under the impression that it may not be helpful which is again a wrong attitude.
- The branch auditor should realise and recognise the fact that his work and comments on the branch is of immense help to the central auditor in the audit of the bank as a whole.
- Branches are the field offices where the actual operations take place and what a SCA is to a bank, SBA is to a branch and only with the support of the SBAs, SCAs can do a proper exercise of audit reporting.

PLANNING

- SA 300 (Revised) “Planning an Audit of Financial Statements”
- The objective of the auditor is to plan the audit to perform in an **effective** manner.
- A few branches may be distant branches and missing out covering some important aspect cannot be set right on a later date.
- It is a group effort wherein the engagement partner and other key members of the team shall be involved in planning the audit – experience and insight enhance the efficiency.
- Communicating with previous auditor in compliance with relevant ethical requirements.
- To identify and assess the risk to the firm in accepting or continuing with an engagement.
- To review the firm’s ability to perform the engagement regarding the availability of qualified staff, need for specialized assistance, any conflicts of interest, if any – SA 220 is on “Quality Control for Audit work” is relevant.

PLANNING ACTIVITIES

- The process of establishing the overall audit strategy assists the auditor to determine, subject to auditors risk assessment procedures such as:
 - The resources and their type and number to be deployed for specific audit areas considering their experience – NPAs, scrutiny of stock statements, ledger scrutiny, perusal of loan files and documents, LFAR etc.
 - To manage such resources by direction, supervision review and resolution of issues including quality control.

- Overall audit strategy and audit plan are closely inter related – however planning is more detailed and continues to depend upon developments. Eg. CBS based NPAs
- The presence of a partner is necessary throughout the audit particularly in the medium, large and very large branches. In very large branches presence of two partners or one partner and a qualified assistant, may facilitate taking appropriate and objective views / judgements.

COMMUNICATION WITH PREVIOUS AUDITOR

- To safeguard his interest and that of public
- Independence
- To know the reason for not accepting the appointment, if any like qualification, legitimate fees not paid etc.

TERMS OF AUDIT ENGAGEMENTS (TOE)

- TOE to be documented in order to cement the terms to be agreed in relation to the audit
- TOE assists in understanding as to the objectives and scope of the audit engagement the extent of management's responsibilities and its own responsibilities so as to minimise the risk that the bank may rely on the auditors inappropriately to protect the entity against certain risks or to perform certain functions that the auditors consider to be client's responsibility.

FORM AND CONTENT OF TOE:

- Objectives of audit.
- Management responsibility for the financial statements including selection and consistent application of appropriate accounting policies and Accounting Standards besides making judgments and estimates that are reasonable and prudent.
- Management responsibility for maintenance adequate accounting records and internal controls for safeguarding of assets.
- Commitment to compliance with applicable legislation, regulation and pronouncements of RBI and ICAI regarding NPAs etc.
- Unrestricted access to records, documents and other information related to audit.
- The fact that the audit process may be subjected to a peer review under the CA Act, 1949.
- Requesting the Bank to confirm in writing the representations besides confirming the TOE by acknowledging the receipt of engagement letter.

BANK AND ITS ENVIRONMENT

- SA 315 – “Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and Environment”.
- Discussion with the management.
- Discussion with the internal / concurrent auditors and review of their reports besides legal and other advisors.
- RBI guidelines and inspection reports.
- Review of closing instruction / circulars.
- Level of computerization – CBS. At branch audit level it is difficult to have access to the overall IT policy, process controls and accounting procedures but primary records and entry level transaction can be accessed, substantive checking of sample transactions be resorted to. Besides periodical MIS and exception reports verification, hard copies can be called for.
- The use of IT in banks affects the way control activities are implemented.
- From the auditors’ perspective, controls over IT system are effective when they maintain the integrity of the information and the security of the data such systems process and includes effective IT controls and application controls.
- To identify the risks while understanding the entity and its environment including relevant controls that relate to risks.
- To assess the identified risks and evaluate as to what can go wrong at the assertion level for classes of transaction, account balances and disclosures including accounting policies in the financial statements.
- To consider the likelihood of a misstatement including possible multiple misstatements or material misstatement.
- To give specific emphasis on the risks arising out of the fraud, changes in regulatory environment, complex transaction, related party transaction and abnormal business transactions.
- The use of professional scepticism and experience acquired during the course of audit, particularly concurrent audits, play a vital role in the process.
- Careful perusal of the concurrent, inspection, revenue, credit audit, RBI Inspections, AQR, Systems audit shall be very handy.

QUALITY CONTROL FOR AUDIT WORK (SA 220)

- Procedures regarding the work delegated to assistants in an audit.

- Policies and procedures of an audit firm regarding audit work generally.
- Professional requirements – Independence, integrity, objective confidentiality and professional behavior, skills, competence – Technical students and professional competence, Assignment of work to appropriate personnel, delegation, consultation, monitoring the adequacy and operational effectiveness of quality control policies and procedures communicating the same to the personnel.
- Delegation of work – Competence
- Direction – Audit programme – Time frame
- Supervising – Assistants have necessary skills, understanding the procedures and directions in consonance with the audit programme and the overall audit plan.
- Review adequately documented Resolution of significant audit matters and audit conclusions in line with results of work performed and support the audit opinion. Eg. NPAs divergence – Restructuring Interest reversals – down / upgrade etc., sector wise classification – MOCs.
- Assessment of inherent and control risks sometimes necessitating alteration of audit plan / programme.

AUDIT PROGRAMME

Guidance Note has given a comprehensive checklist / audit programme for bank branch audit and it can be readily used for carrying out an efficient audit.

- a. Audit of Advances – NPA, LFAR,
- b. Audit of all other items in the Trial Balance (TB).
- c. Ensuring various Compliances like Banks internal closing circular, RBI circular, LFAR, etc.
- d. LFAR – other than advances
- e. Audit of other aspects – Tax audit, certifications, etc.

SA 230 – AUDIT DOCUMENTATION

Audit documentation should be sufficient and enable an experienced auditor, having no previous connection with the audit, to understand:

- a) The nature, timing, and extent of the audit procedures performed to comply with the SAs and applicable legal and regulatory requirements;
- b) The results of the audit procedures performed, and the audit evidence obtained; and
- c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

In documenting the nature, timing and extent of audit procedures performed, the auditor shall record:

- a) The identifying characteristics of the specific items or matters tested;
- b) Who performed the audit work and the date such work was completed; and

c) Who reviewed the audit work performed and the date and extent of such review.

The auditor shall document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place.

If the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter, the auditor shall document how the auditor addressed the inconsistency.

SA 580 – WRITTEN REPRESENTATIONS

A representation letter should be obtained.

Written representations are audit evidence.

Through written representations the management / those charged with governance confirm their belief that they have fulfilled the responsibility for the preparation of the financial statements and for the completeness of information provided to the auditor.

Written representations provide other audit evidence relevant to the financial statements or specific assertions in the financial statements.

When such written representations have not been provided, auditor has to respond appropriately by qualifying the report.

CONCLUSION :

Proper planning would go a long way in doing the audit effectively.

Proper documentation would go a long way in proving that a proper audit exercise has been done.