

Long Form Audit Report and Tax Audit in Respect of Bank Branches

Long Form Audit Report (LFAR), a detailed questionnaire prepared by Reserve Bank of India (RBI), has been in use since 1992–93. It is not an annexure to the Auditors Report but a Management Letter to be addressed to the Bank's Management

to apply the revised format from the year ending March 31, 2003. The revised format mainly focuses on systemic issues in banks, tries to address them through the insight of the bank branch auditors and acts as an early whistle blower for the irregularities persisting in the branch/bank

avoid duplication of work and enable timely completion of the statutory audit function

- Complete and submit the Main Audit Report as well as the LFAR simultaneously
- The responses to questionnaire should be categorical, specific and to the point. The answers should not be only 'Yes/No/Not Applicable'. Vague/general comments should be avoided
- Give instances of shortcomings/weaknesses in the LFAR, wherever possible
- Do not make current year's LFAR a replica of the previous year's LFAR
- The branch LFAR should be addressed to the Bank's Chairman and a copy thereof should be sent to the Central Statutory Auditor
- The Audit Report and LFAR, being two separate and distinct reports, any comments of qualificatory nature should not be included in LFAR. Such Audit Qualifications should be included in the Audit Report and not in LFAR. In deciding whether qualification in the auditors report is necessary, the auditor should use his discretion considering the facts and circumstances of each case
- The Main Audit Report should be a self-contained document and no reference should be made in the Au-

Nilesh S. Vikamsey

Ketan S. Vikamsey

The authors are members of the Institute. They can be reached at nilesh@khimji-kunverji.com

As part of Statutory Audit of Bank Branches, an Auditor is required to answer a detailed questionnaire prepared by Reserve Bank of India (RBI). This report is generally known as "Long Form Audit Report (LFAR)". Under Section 44AB of the Income Tax Act, the entities whose turnover or gross receipts exceed Rs. 40 lacs during a financial year are required to get their accounts audited. This audit is generally known as "Tax Audit". This article focuses on certain aspects of reporting in LFAR and certain issues involved in Tax Audit of Bank Branches.

(Note: The detailed questions/ annexure of LFAR have not been reproduced in this article. Members are advised to go through the Latest Guidance Note on Audit of Banks issued by ICAI for list of questions covered in LFAR and Audit checks to be applied for each question.)

History

The LFAR, which has been in use since 1992–93, was revised in consultation with ICAI and a few selected banks' representatives to reflect changes in regulatory/supervisory framework of banks as also the expanded role of statutory auditors who are now required to include certain additional certification/ validations in their report. Banks were advised

General

Prior to responding to the questions of LFAR, branch auditors need to consider the following:

- The LFAR Questionnaire is an excellent Audit Planning Tool, based on which the auditor may decide the areas to be covered by their audit team members
- Studying the LFAR Questionnaire thoroughly beforehand gives an insight to the audit team of the areas involved in bank audit as well as in deciding the time to be allocated in respect of each area
- The work on LFAR should be started along with statutory audit right from day one in order to

The questions in LFAR in respect of Bank Branches are divided into four major categories viz. Assets, Liabilities, Profit & Loss Account and General

- The LFAR should be sufficiently detailed and quantified in order to expeditiously consolidate the same for the bank as a whole.

Questionnaire

The questions in LFAR in respect of Bank Branches are divided into four major categories viz. Assets, Liabilities, Profit & Loss Account and General.

Significant Audit Checks in respect of LFAR

Auditor needs to take extra care while responding to the questions in LFAR. Significant audit checks required for responding to certain questions in LFAR are given here in Table - A :

Questionnaire Applicable to Specialised Branches

In addition to the questionnaire discussed above, RBI has prepared separate questionnaire for certain specialised branches dealing in-

- Foreign Exchange Transactions
- Very large advances such as Corporate Banking Branches and Industrial Finance

forming Assets such as Asset Recovery Management Branches

- Clearing House Operations, Normally Referred to as Service Branches

Since the above-referred branches deal in specialised areas of banking, auditor also needs to pay extra attention while responding.

Advances

As we are aware, Advances form a very important part of Banking Business and the auditor needs to pay special attention. Auditors are required to obtain details of large/irregular/critical advance accounts in case of branches dealing in large advances/asset recovery branches, in the specified format enclosed as part of annexure to the LFAR. For verification of other advances, the auditor can use the following illustrative checklist, which lists out various irregularities persisting in respect of advances:

Advances Checklist for LFAR

1. In respect of common irregularities, the Auditors can give borrower-wise comments in the format given hereunder:

| Name of Borrower | Name of Branch | Region | IRAC Status | Sanctioning Authority | Facility | Limit | Amount o/s. as at year end | Irregularity No. |
|------------------|----------------|--------|-------------|-----------------------|----------|-------|----------------------------|------------------|
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |

- Branches or Branches with advances in excess of Rs.100 crore.
- Recovery of Non-Per-

2. In respect of Column 9 above, "Irregularity No.", the number as given in the "Glossary to Irregu-

3. The borrower-wise details may be given in descending order based on the Amount outstanding

Table - A

| Question | Significant Audit Checks |
|--|--|
| <p>Advances (Sanctioning/Disbursement) In the cases examined by you, have you come across instances of credit facilities having been sanctioned beyond the delegated authority or limit fixed for the branch? Are such cases promptly reported to higher authorities?</p> | <p>Obtain Operations Manual/Circulars prescribing delegated authority or limits of the branch officials. Whether telephonic sanctions by higher authorities are followed up by written confirmations. Whether Adhoc limits (increase) granted to borrowers for temporary/easonal/peak periods are periodically reported to controlling authorities and whether the same is liquidated within the stipulated time</p> |

| | |
|--|--|
| In the cases examined by you, have you come across instances where advances have been disbursed without complying with the terms and conditions of the sanction? If so, give details of such cases | Strongly report non-compliance and non-repayment. Examples/instances of not implementing terms and conditions of sanction are given in Point no 2 of Glossary of Irregularities. |
| Advances (Documentation) In respect of advances examined by you, have you come across instances of deficiencies in documentation, non-registration of charges, non-obtaining of guarantees, etc.? If so, give details of such cases | Examples/instances of deficiencies in documentation, non-registration of charges, non-obtaining of guarantees, etc. are given in Point no 3 of Glossary of Irregularities. The auditors should not put audit ticks on legal documents to avoid legal complications in future |
| Advances (Review/Monitoring/Supervision) Are the stock/book debt statements and other periodic operational data and financial statements, etc., received regularly from the borrowers and duly scrutinised? Is suitable action taken on the basis of such scrutiny in appropriate cases? | <ul style="list-style-type: none"> ● Whether stock/book debt statements are being received regularly? If not, report ● Whether the same are being critically scrutinised for non-moving/obsolete/damaged stock and action taken thereon? ● Whether such year-end stock/book debt statements compared to the audited Balance Sheet to ascertain variance in Stocks/book debts? ● How are the stock/book debts more than three months considered for DP and for classifying the loans (secured/unsecured)? |
| Has the branch identified and classified advances into standard/substandard/doubtful/ loss assets in line with the norms prescribed by the Reserve Bank of India (The auditor may refer to the relevant HO Instructions for identification of NPAs and Classification of Advances) | <ul style="list-style-type: none"> ● On some issues, Bank Circular may interpret differently from the intention of RBI Circulars. Rely on RBI Circulars ● If auditor does not agree to any classification, mention detailed reasons and include in MOC and Main Audit Report |
| List the major deficiencies in credit review, monitoring and supervision | Examples of major deficiencies in credit review, monitoring and supervision are given in Point no 4 of Glossary of Irregularities. |
| Other Assets (Stationery and Stamps) Does the system of the Bank ensure adequate internal control over issue and custody of stationery comprising security items (Term Deposit Receipts, Drafts, Pay Orders, Cheque Books, Traveller's Cheques, Gift Cheques, etc.)? Whether the system is being followed by the branch? | Understand the system of issue and custody of stationery. The system will highlight the method adopted by the branch in the use and safe-custody of stationery. After being satisfied about the system being adopted by the branch, the auditor may check the implementation of the system and report on non-implementation of such systems, if any |
| Have you come across cases of missing/lost items of such stationery? | <ul style="list-style-type: none"> ● Mention details of missing/lost items of stationery (e.g. Drafts) ● Inform central statutory auditors to check provisioning there against, if encashed fraudulently |
| Deposits After the balance sheet date and till the date of audit, whether there have been any unusual large movements (whether increase or decrease) in the aggregate deposits held at the year-end? If so, obtain the clarifications from the management and give your comments thereon | Apply cut-off procedure to ascertain any unusual large movements in deposits. To determine probable window dressing, if any |
| Contingent Liabilities List of major items of the contingent liabilities (other than constituents' liabilities such as guarantees, letters of credit, acceptances, endorsements, etc.) not acknowledged by the Branch? | <ul style="list-style-type: none"> ● Contingent liabilities, being an important "off balance sheet" item, seek reasonable assurance that all contingent liabilities are identified and properly disclosed. For e.g. Increase in rent of premises by landlord disputed by bank ● Obtain a letter of representation to the effect that there are no contingent liabilities existing in the branch other than those disclosed in the financial statements |
| Profit and Loss Account Whether the branch has a system to compute discrepancies in interest/ discount and for timely adjustment thereof in accordance with the guidelines laid down in this regard by the controlling authorities of the bank? Has the test checking of interest revealed excess/short credit of a material amount? If so, give details thereof | <ul style="list-style-type: none"> ● The branch should have a system of verification of interest and discount so as to be able to detect discrepancies: Maker-Checker concept ● Verify that adjustments of discrepancies have been done in accordance with the laid down guidelines ● In case discrepancies exist in large number of cases taken for test checking, the auditor should consider its impact on the accounts and ascertain whether qualifying Auditors Report would be required. For this purpose, get the total amounts quantified from the Branch Officials and selectively verify its veracity <p>Review revenue audit/concurrent audit reports for any short/excess recoveries, reasons thereof and remedial measures taken to avoid repetition of mistakes</p> |

| | |
|---|--|
| <p>Are there any divergent trends in major items of income and expenditure, which are not satisfactorily explained by the branch? If so, the same may be reported upon. For this purpose, an appropriate statement may be obtained from the branch management explaining the divergent trends in major items of income and expenditure</p> | <ul style="list-style-type: none"> ● One point deleted from old LFAR but should be reported by Branch auditors as part of normal audit procedure is “Indicate the effect of changes, if any, in accounting policies on the items of Income & Expenditure” ● For identified divergent trends, obtain supporting evidences like monthly weighted average figures, composition of the income/expenditure, etc. |
| <p>General (Books and Records) In respect of computerised branches: Whether hard copies of accounts are printed regularly?</p> | <p>The main difficulty would be in tracking back Changes made in soft copies in case hard copies are not taken</p> |
| <p>Indicate the extent of computerisation and the areas of operation covered</p> | <p>Check if Information Systems Audit is conducted and that its report is satisfactory</p> |
| <p>Are the access and data security measures and other internal controls adequate?</p> | <p>Refer to Guidance Note on Audit of Banks issued by ICAI (August 2005 – Page No. 115)</p> |
| <p>General (Inter Branch Accounts) (i) Does the branch forward on a daily basis to a designated cell/ Head Office, a statement of debit/credit transactions in relation to other branches? (ii) Does a check of the balance in the Head Office Account as shown in the said statement during and as at the year-end reveal that the same is in agreement with the Head Office Account in the general ledger? (iii) Are there any outstanding debits in the Head Office Account in respect of inter-branch transactions? (iv) Does the branch expeditiously comply with/respond to the communications from the designated cell/Head Office as regards unmatched transactions? As at the year-end are there any unresponded/uncomplied queries or communications? If so, give details? (v) Have you come across items of double responses in the Head Office Account? If so, give details (vi) Are there any old/large outstanding transaction/entries at debits as at year-end which remain unexplained in the accounts relating to inter-branch adjustments?</p> | <p>Being a back-office function, Inter Branch Reconciliation (IBR) is generally seen as a neglected area. The auditor needs to critically understand the IBR system prevalent in the branch and accordingly prepare an audit plan to review the IBR transactions. The large volume of Inter Branch Transactions and unreconciled entries in the banking system makes the area fraud-prone. Check the head-office inward communication to branch to ascertain date upto which statements relating to inter-branch reconciliation have been sent. Check and Report:</p> <ul style="list-style-type: none"> ✓ Reversal of any large/old/unexplained entries, which had remained outstanding in IBR ✓ Items of revenue nature, cash-in-transit (for example, cash meant for deposit into currency chest) which remains pending for more than a reasonable period ✓ Double responses to entries in the Accounts <ul style="list-style-type: none"> ● Test Check accuracy and correctness of “Daily statements” prepared by the branch and sent to IBR department ● Tabulate and report pending entries over two years into: Year, No. of Entries, Total Amount, Average Amount ● If outstanding debits in HO Account are not confirmed/recorded by HO, review critically and recommend provision for e.g. unrecorded revenue expenses, etc. ● Based on the review of details and norms of RBI with respect to IBR transactions, the auditor should consider the extent of non-reconciliation in forming his opinion on the financial statements. Where the amounts involved are material, the auditor should suitably qualify his audit report. Attention is drawn on the paper on “Certain Significant Aspect of Statutory Audit of banks” issued by the Council of ICAI in March, 1994, published in the CA journal ● Further, vide circular no. DBOD No. BP/BC. 73/21.04.018/2002-03 dated February 26, 2003, the RBI advised the banks to maintain category-wise (head-wise) accounts for various types of transactions put through inter-branch accounts so that the netting can be done category-wise. Further, RBI advised banks to make 100 per cent provision (category-wise) for net debit position in their inter-branch accounts arising out of unreconciled entries, both debit and credit, outstanding for more than six months |
| <p>Does the branch maintain records of all the fixed assets acquired and held by it irrespective of whether the values thereof or depreciation thereon have been centralised? Where documents of title in relation to branch or other branches are available at the branch, whether the same have been verified</p> | <p>Generally, branches do not have power to purchase fixed assets. Nonetheless, branches are obliged to maintain the records of fixed assets existing at the branch, though accounting entries thereof are maintained at controlling/ head office. Documents of title in relation to branch's fixed assets have to be maintained at the branch and verified by the auditor</p> |

4. Glossary to Irregularities

| Item | Audit Remark |
|----------|--|
| 1 | Credit Appraisal |
| 1.1 | Loan application not on record at Branch |
| 1.2 | The appraisal form was not filled up correctly and thereby the appraisal and assessment was not done properly |
| 1.3 | Loan application is not in the form prescribed by Head Office |
| 1.4 | The Bank did not receive certain necessary documents and Annexures required with the application form |
| 1.5 | Basic documents such as Memorandum & Articles of Association, Partnership deed, etc, which are a pre-requisite to determine the status of the borrower, not obtained |
| 1.6 | Certain adverse features of the borrower not incorporated in the appraisal note forwarded to the management |
| 1.7 | Industry/group exposure and past experience of the Bank is not dealt with in the appraisal note sent to the management for sanction |
| 1.8 | The level for inventory/book-debts/creditors for finding out the working capital is not properly assessed |
| 1.9 | Techno-economic feasibility report, which is required to know the technical aspects of the borrower's business, is not obtained from Technical Cell. |
| 1.10 | Credit report on principal borrowers and confidential report from their banks are not insisted from the borrowers. |
| 1.11 | The opinion reports of the associate and/ or sister concerns of the borrower are not scrutinised |
| 1.12 | The opinion reports of the associate and/ or sister concerns of the borrower are not called for |
| 1.13 | The opinion reports of the associate and/ or sister concerns of the borrower are not updated |
| 1.14 | The opinion reports of the associate and/ or sister concerns of the borrower are not satisfactory |
| 1.15 | The opinion reports of the associate and/ or sister concerns of the borrower are not scrutinised/ not called for/ not updated/ not satisfactory |
| 1.16 | The procedure/ instructions of head office regarding preparation of proposals for grant not followed |
| 1.17 | The procedure/instructions of head office regarding preparation of proposals for renewal of advances not followed |
| 1.18 | The procedure/instructions of head office regarding preparation of proposals for enhancement of limits, etc. not followed |
| 1.19 | No exposure limits are fixed for forward contract for foreign exchange sales/purchase transactions |
| 2 | Sanctioning and Disbursement |
| 2.1 | Credit facility sanctioned beyond the delegated authority or limit of the branch |
| 2.2 | Certain proposals were sanctioned pending approval of higher authorities wherever required |
| 2.3 | Ad-hoc limits were granted for which sanctions were pending since long |
| 2.4 | Facilities were disbursed before completion of documentation |
| 2.5 | Facilities were disbursed without following sanction terms |
| 2.6 | Facilities were disbursed without any sanction |
| 2.7 | Sanction letter was missing in the branch |
| 2.8 | Guarantor as required in the sanction letter was not obtained |
| 2.9 | Required promoters stake not invested before disbursement of loan |
| 2.10 | Sanctions were made without proper appraisal |
| 2.11 | Security charge not created before disbursement as required by sanction letter/renewed letter |
| 2.12 | Full disbursement of the facility not made |
| 2.13 | Sanction terms were not complied with or were not recorded |
| 2.14 | Disbursement Made without proper sanction |
| 2.15 | Term loan was disbursed by creating the cash credit or savings account of the borrower |
| 3 | Documentation |
| 3.1 | The security against which the advance was sanctioned was not available/was not on record |
| 3.2 | Mortgage for the property given as security is not created |

| | |
|----------|--|
| 3.3 | Mortgage for the property given as security created, was inadequate, as compared to terms of sanction |
| 3.4 | Second charge as required on assets is not created in favour of the bank |
| 3.5 | Documents of Second charge on assets is not on the record |
| 3.6 | Documents pertaining to registration of charges with ROC or any other authority concerned requiring charging of assets is not obtained |
| 3.7 | Copies evidencing lodgment of the original conveyance/ sale deeds with the Sub-Registrars for registration not on record |
| 3.8 | Authority letter/Power of Attorney to the Bank to collect the original documents from the Sub-Registrar not on record |
| 3.9 | Documents pertaining to consortium advances not yet executed/not available with bank |
| 3.10 | Documents signed by persons not duly authorised to sign or who have signed in other capacity accepted by the bank |
| 3.11 | Signatures of the executants were not found on all the pages of the documents |
| 3.12 | Some of the documents on record were blank, without signatures of Branch Manager, witnesses, or guarantors, etc. |
| 3.13 | Revival letters in respect of documents to be reviewed from the borrowers not received |
| 3.14 | Guarantors have expired |
| 3.15 | Guarantors not on record |
| 3.16 | Guarantors not renewed |
| 3.17 | Guarantors not assigned |
| 3.18 | Worth of the Guarantors not available |
| 3.19 | Stamping not as per the amended Stamps Act |
| 3.20 | Documents have become mutilated, soiled, time barred or not obtained |
| 3.21 | Opinion report by the field officer for the borrowers not found on record |
| 3.23 | “Nil Encumbrance Certificate/s” or “No Dues Certificate/s” or “No lien Letters” not obtained for the mortgage/s |
| 3.24 | Advances for vehicle loans, Registration certificate, transfer certificate, etc. not obtained |
| 3.25 | Work completion certificate, sale deeds, share certificates in societies, etc. not on record for housing loans |
| 3.26 | Documents are not duly attested/ signed by concerned officials/ not renewed |
| 3.27 | The agreements for hypothecation do not contain details regarding goods hypothecated |
| 3.28 | Copy of Bills/ receipts, on the basis of which the amount was disbursed not found on record. For e.g. Vehicle Loans, Plant & Machinery |
| 3.29 | Charge on main &/ or collateral securities not created in terms of sanction letter |
| 3.30 | Original security papers/sale deed/lease deed/title deed/agreement of sale not available on record |
| 3.31 | TDR are not discharged or renewed |
| 3.32 | Control returns not sent to the HO |
| 3.33 | The branch has not taken any action for not compliance with terms of agreement |
| 3.34 | No documents executed for enhancement of limit/document not on record |
| 3.35 | ECGC post-shipment policy not obtained |
| 3.36 | Credit facility released without execution of all necessary documents |
| 3.37 | Common Seal not affixed on Letter of Comfort |
| 3.38 | Confirm orders for export credit not found on record for facilities released |
| 4 | Review/Monitoring/Supervision |
| 4.1 | The account is frequently overdrawn |
| 4.2 | The account is continuously overdrawn |
| 4.3 | The account is overdrawn and the branches have not taken sufficient steps to regularise the accounts promptly |
| 4.4 | The balance outstanding have exceeded the drawing power |
| 4.5 | Balance confirmation and acknowledgment of debt not obtained |
| 4.6 | The stock, book-debts statements not received regularly/promptly |
| 4.7 | The FFI/financial statements/audited statements/FFR 1 & 2/other operational data, etc., not received regularly/promptly |

| | |
|------|--|
| 4.8 | The stock, book-debts statements, etc., not scrutinised and no suitable action is taken |
| 4.9 | The FFI/financial statements/ audited statements/ FFR 1 & 2/ other operational data, etc. not received regularly/promptly/ not scrutinised and no suitable action is taken |
| 4.10 | Non-moving stock is not deducted to arrive at the drawing power |
| 4.11 | The age-wise break-up of debtors is not found on record. The borrowers are allowed to draw money on entire outstanding debt, which must rather be for the recent debts as prescribed for particular industries and as per margin prescribed in the sanction letter |
| 4.12 | Wide discrepancies observed in the stock statements and stock figures in the annual audited financial statements |
| 4.13 | No penal interest has been charged for delay in submission of various statements as per the terms of agreement depending upon the type of loan/credit availed by the borrower |
| 4.14 | Many branches have not adhered to the prescribed frequency of physical verification of securities given against loans & advances |
| 4.15 | Drawing power limits are not revised as per market value of shares for advances against security of shares |
| 4.16 | End-use of funds not ensured/not known funds utilised for purpose other than for which granted |
| 4.17 | The projections submitted by the borrower stay far beyond the actual performance. Further, no explanation for the same is taken from the borrower |
| 4.18 | Major sale proceeds of the borrower not routed through the Bank |
| 4.19 | Audited statements of non-corporate borrowers having limit beyond Rs.10 lakh not received |
| 4.20 | Renewal proposals of advances not received on time and in many cases the limits are not renewed |
| 4.21 | Application of wrong rate of interest, processing charges, commission, other charges, etc. resulting in income leakage/excess booking of interest of the Bank. |
| 4.22 | Insurance cover for stock/property is inadequate/not on record/not renewed/not endorsed in favour of the Bank |
| 4.23 | Inspection/physical verification of security charged, not been carried out |
| 4.24 | Expired bills/foreign currency sight bills which are outstanding, have not been crystallised |
| 4.25 | EBW statements on write-off of overdue export bills of ECM not found on record |
| 4.26 | Confirmation as to genuineness of export transactions not obtained from Bank's foreign offices/ correspondents/customs department |
| 4.27 | Import credit, bill of entry evidencing import of goods not found |
| 4.28 | Documents are not obtained for bills discounted under Letter of Credit |
| 4.29 | Advances, which are eligible for whole turnover packing credit guarantee cover of ECGC, are not brought under its cover |
| 4.30 | Though government guaranteed accounts are irregular since long, the issue of invocation of guarantee does not seem to have been considered |
| 4.31 | Prescribed margins not maintained as per sanctions |
| 4.32 | Allocated limits, full terms of sanctions, stock statements, inspection reports, margin, etc. not available at monitoring branches |
| 4.33 | For allocated limits, inordinate delays were noticed in responding to transfer by the allocator branch |
| 4.34 | Regular meetings not held with other consortium members to review the performance of borrowers and to assess the current state of affairs/not been held as per norms |
| 4.35 | Individual members of the consortium are not advised about the quarterly operating limits/D.P. allocated to each one of them |
| 4.36 | Minutes of the consortium meetings not found on record/not been held as per norms |
| 4.37 | Inspection report from the consortium members not obtained |
| 4.38 | The capital of the borrower has eroded/networth is negative/decreasing. Close monitoring needs to be done |
| 4.39 | The drawing power is calculated wrongly and/or hence the borrower is allowed to enjoy excess credit than actually eligible |
| 4.40 | Signboard of the bank is not displayed in godown, where the pledged/hypothecated stock is stored |
| 4.41 | Limit not fully utilised by the borrower/no commitment charge is levied for the limit not fully utilised by the borrower |
| 4.42 | Loan against TDR/STDR, which is matured, is neither renewed nor credited to loan account |
| 4.43 | The Stock and Debtors Audit Report not found on record. No audit has been done for accounts of the borrower |

| | |
|----------|--|
| 4.44 | The valuation report in respect of tangible security from government approved valuer have not been obtained |
| 4.45 | Guarantees, Opinion Reports, Financial statements, IT assessment orders and etc. of the guarantor are not found on record |
| 4.46 | Opinion report on guarantor is not obtained |
| 4.47 | For Small Government Sponsored loan accounts, security cover could not be ascertained since neither any record was available at branch nor physical verification conducted by the branch |
| 4.48 | Pre-sanctions and/or post-sanctions inspection reports were not on record |
| 4.49 | The account was overdue for repayment and/or no credit was received from the borrower for a long time |
| 4.50 | The borrower is absconding or deceased and legal formalities are incomplete and there is wilful default from the borrower. Either establishment was closed or security was disposed off or no action taken by the branch |
| 4.51 | Subsidy claim process was incomplete or subsidy was yet to be received or needs follow-up |
| 4.52 | Security disposed off/Entity closed by borrower and no action taken by the branch |
| 4.53 | Irregularity not advised to controllers |
| 4.54 | Letter of subordination of deposits not taken |
| 4.55 | Secured and unsecured portion not segregated properly in advance return of the branch |
| 4.56 | Renewal of limits was done before the receipt of financial statements |
| 4.57 | Heavy cash withdrawal for which consent of corporate Guarantor is not taken |
| 4.58 | Proper valuation of stock not done/ needs critical scrutiny |
| 4.59 | Security obtained is inadequate/ lower as compared to amount of outstanding/ no collateral security |
| 4.60 | The party was dealing with other bank also though it was not permitted |
| 4.61 | Sticky accounts require close follow-up by the management |
| 5 | Bad and Doubtful Advances |
| 5.1 | The IRAC norms for classification of advances were not followed and the same is implemented through Memorandum of Changes by auditors during audit |
| 5.2 | Installments were not received from the borrowers |
| 5.3 | Interest was not received from the borrowers |
| 5.4 | Legal action for recovery of advances was not taken although authorised by the Board/ Controlling Authority |
| 5.5 | Discontinuance of application of interest not followed although authorised by the Board/ Controlling Authority |
| 5.6 | Government guarantees have expired and fresh guarantees not obtained/not renewed |
| 5.7 | Terms of the BIFR scheme not complied |
| 5.8 | Payment from government not received although guarantees were unconditional, irrevocable and payable on demand |
| 5.9 | Delays in the settlement/repayment in respect of sanctioned proposals |
| 5.10 | The repayment accepted in case of compromise cases inadequate vis-à-vis value of security |
| 5.11 | Compromise proposals pending at various levels where local government/outside agencies are involved as guarantors |
| 5.12 | Copy of Search Report not on record |
| 5.13 | Decree awarded but no further steps taken for recovery |
| 5.14 | DI&CGC claims submitted/ rejected/ pending data not available |
| 5.15 | Irregular/ sticky advance not reported to the controlling authority promptly |
| 5.16 | Compromise/ OTS proposal is recommended and is under negotiation since long but not finalised. Suit is filed in the court/ DRT and pending to be finalised |
| 5.17 | ECGC claim not submitted/lodged for recovery |

TAX AUDIT

Background

Every Banking Company is liable for Tax Audit with the objective of expressing an opinion on the financial statements and verifying the statement of particulars prepared in the prescribed form as required under section 44AB of the Income-Tax Act, 1961 and Rule 6G of Income-tax Rules, 1962

(Note: The detailed Form 3CA/3CD have not been reproduced in this article. For further details, members are advised to go through the Income Tax Act/Rules and the Latest Guidance Note on Tax Audit under section 44AB of the Income Tax Act issued by ICAI)

General

Accounts department at Head Office of a Bank circulates a format of Tax Audit Report/Statement of particulars in which they require details under various applicable clauses of Form 3CD along with specific guidelines. Prior to replying in the circulated format, branch auditors need to consider the following:

- ✓ Critically Study the circulated format by HO and Compare the same with standard clauses of Form 3CD. Generally, it is observed that such circulated formats have pre-printed replies, which may not necessarily match with the response that the auditor would like to give, for e.g., the auditor may like to qualify a clause in case data relating to such clause is not in conformity with the requirements of such clause. In such case, the auditors need not be carried away with such pre-printed response and give his own response explaining the factual situation.

It is recommended that before finalising the LFAR and Tax Audit report, the auditor should discuss it with the branch management, so as to avoid any incorrect reporting

- ✓ Further, such format circulated by HO contains certain clauses which states “Not Applicable (N.A.)” (for e.g. responses to clauses relating to section 40A(2)(b), 40A(ia), 269T – Repayment of Deposits, Ratios, TDS, etc. may be pre-printed “N.A.” as per HO. However, the branch auditor needs to independently make his own judgment in such cases and report)
- ✓ Some banks ask for details relating to only specific clauses of Form 3CD instead of fully reproducing Form 3CD. In such a scenario, the auditor needs to be extra careful and understand the report, which he is required to give along with such details relating to Form 3CD. In case such

report is in a format similar to Form 3CA, he should qualify the same, specifying non-furnishing of data, if any, relating to certain clauses of Form 3CD, due to non-availability of data from the bank.

- ✓ Plan the Tax Audit work along with the statutory audit and have a detailed Checklist ready prior to commencement of audit.
- ✓ Obtain detailed Management Representation Letter from the Branch Management.

Specific Reporting

In certain clauses, where it is not possible for the Auditors to categorically comment, he may give the following notes against the specific clauses, suitably modifying the same based on extant circumstances (See Table - B).

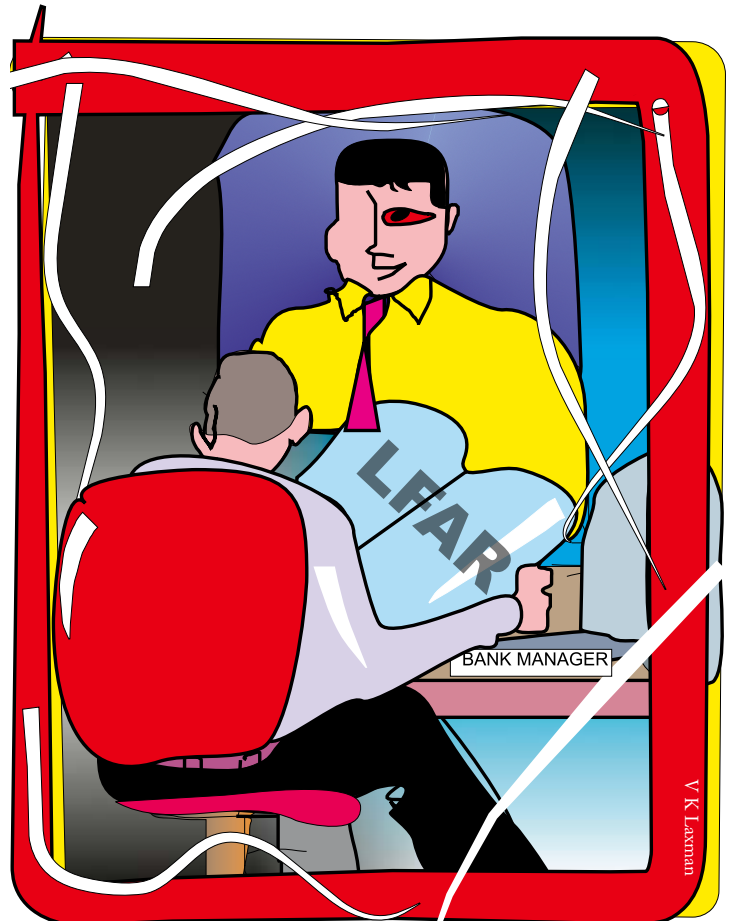


Table - B

| Clause | Particulars | Auditors' Note |
|------------|--|---|
| 17(b) | Amount debited to profit and loss account— expenditure of personal nature | “On the basis of our examination of books of accounts, the vouchers produced to us for verification, the explanations given and representations made to us on our inquiries and the check and control relating to authorising the expenditure on the basis of contractual obligations to the employees/directors, accepted business practices having regard to the Branch’s needs and exigencies, we have not come across any expenses charged to Revenue, which in our opinion and judgment and to the best of the knowledge and belief, could be regarded as personal expenses” |
| 17(e)(iii) | Amount debited to profit and loss account— Expenditure incurred for any purpose which is an offence or which is prohibited by law | “We have not come across any expenditure incurred for any purpose which is an offence or which is prohibited by law and the same is also confirmed by the branch management” |
| 17(h) | Amount debited to profit and loss account— Amounts inadmissible under 40A(3) read with rule 6DD and the computation thereof | “It is not possible for us to verify whether the payments made through bank in excess of Rs. 20,000 have been made otherwise than by crossed cheque or by crossed bank draft due to the huge volume of transactions. The branch management, however, confirms that all payments made in excess of Rs. 20,000 have been made by crossed cheque or by crossed bank draft” |
| 21(ii) | Details of actual payment with respect to Contribution to Provident Fund/Superannuation Fund/ Gratuity Fund/ Other fund for the welfare of employees | <p>“Clause 21(ii)(B)(b) requires mentioning the due date of payment under second proviso to section 43B (as existing up to AY 2003–04), which provided that no deductions shall be allowed in respect of sums referred to in clause (b) unless such sum had duly been paid on or before the due dates by which the employer is required to credit employee’s contribution to the relevant employee’s welfare fund account under the respective Acts and when such payment has been made otherwise than in cash, the sum has been realised within 15 days from due date.</p> <p>However, second proviso to section 43B has been omitted by Finance Act, 2003 w.e.f. April 1, 2004 (AY 2004–05). Consequently, deductions shall be allowed in respect of sums referred to in clause (b) if they have been paid on or before the due date of filing return of income u/s. 139(1). Accordingly, the due dates under the respective Acts have not been mentioned against the payments made and ‘whether amount has been realised within 15 days or not if paid otherwise than by cash’ has not been mentioned”</p> |
| 24(b) | Particulars of each repayment of loan or deposit in an amount exceeding the limit specified in section 269T made during the previous year | “It is not possible to verify the details of Term Deposits where repayment over Rs. 20,000 (including interest) is made by Cash, due to huge volume of transactions. The branch management, however, confirms that it has not made any repayment of term deposits over Rs. 20,000 by Cash during the year”. |

Conclusion

LFAR and Tax Audit are vast areas and are to be done along with the normal course of Bank Audit. ICAI has issued Guidance Note on both the above-referred subject, which have been periodically revised. In addition, ICAI and

its regions/branches conduct a number of seminars on the subject for the benefit of its members and students.

It is recommended that before finalising the LFAR and Tax Audit report, the auditor should discuss it with the branch management, so

as to avoid any incorrect reporting. The auditor should also obtain the signature of the branch manager on the above-referred reports after it is finalised to signify acceptance of the comments made therein by the branch management. □