

Draft Manual on Concurrent Audit of Banks

The Internal Audit Standards Board of The Institute of Chartered Accountants of India (ICAI) invites comments on the draft Manual on Concurrent Audit of Banks.

Comments are most helpful if they indicate relevant paragraph number, a clear rationale and, where applicable, provide a suggestion for alternative wording.

Comments can be submitted at link: <https://forms.gle/ECzUfZhLnsV2hR5NA>

Last date for sending comments is October 24, 2025.

Manual on Concurrent Audit of Banks

Disclaimer:

The views expressed in the Manual are those of the authors. The Institute of Chartered Accountants of India may not necessarily subscribe to the views of the author(s).



Internal Audit Standards Board
The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

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Foreword

Preface

Foreword

In India, Banking Sector plays an important role in the development of the economy. The Government has focused on expanding banking coverage in India through various schemes such as Pradhan Mantri Jan Dhan Yojana and Post Payment Banks, etc. With these schemes, combined with key banking sector reforms such as digital payments, neo-banking, the rise of Indian NBFCs, and fintech, have considerably improved the India's financial ecosystem and helped to fuel the country's credit cycle.

This changing landscape in banking sector has put more emphasis on risk management and control functions and made the role of concurrent Auditors very important.

The Manual on Concurrent Audit of Banks is being issued by the Board of Internal Audit and Management Accounting (BIAMA) of the Institute of Chartered Accountants of India (ICAI) with the objective to provide detailed guidance to the members on concurrent audit of banks. I am happy to note that the Board has come out with this revised and updated 2023 edition of "Manual on Concurrent Audit of Banks" for benefit of the members and stakeholders at large.

I compliment CA. Rajendra Kumar P., Chairman, CA. Charanjot Singh Nanda, Vice Chairman, and other members of the Board of Internal Audit and Management Accounting of ICAI for bringing out this revised Manual to assist the members in maintaining quality in concurrent audit of banks.

I am confident that the members and other stakeholders would find this Manual highly useful in their professional assignments.

September 4, 2023
New Delhi

CA. Aniket S. Talati
President, ICAI

Preface

Scarce resources, increased liquidity risk, high complexity and need of integrated management of banking assets and liabilities are shaping banking sector. In the changed scenario, the role of concurrent audit has become even more critical and important for the banks in carrying out operations properly and efficiently. Concurrent audit is essentially a management process integral to the establishment of sound internal accounting functions and effective controls and setting the tone for a vigilant internal audit to preclude the incidence of serious errors and fraudulent implications. Concurrent audit in banks must add demonstrable value in the current competitive banking environment and meet the increasing expectations of regulators, government and professional bodies reflecting the growing importance placed on the function.

As a part of its initiatives to assist the members in understanding the intricacies of concurrent audit and thereby improve the quality of concurrent audit reports, the Board of Internal Audit and Management Accounting of the Institute of Chartered Accountants of India is issuing Manual on Concurrent Audit of Banks (2023 edition). RBI has issued revised Concurrent Audit Guidelines in September 2019. Keeping this in view, the Board has thoroughly revised “Manual on Concurrent Audit of Banks” which has been issued in 2016. Apart from taking impact of above-mentioned guidelines and other related new circulars/ directions issued by RBI, the Board has revised thoroughly Concurrent Audit Checklist.

This Manual provides guidance to members regarding critical issues related to concurrent audit of banks, including redirecting the scope of concurrent audit to include risk-based audit approach to make it more meaningful and effective.

We are immensely grateful to CA. V. Ravindran, CA. Mony Anantasivan and CA. S. Dhayanidhi for sharing their experience and knowledge in review and revising Manual on Concurrent Audit of Banks.

We would like to thank CA. Aniket S. Talati, President, ICAI and CA. Ranjeet Kumar Agarwal, Vice President, ICAI for their continuous support and encouragement to the initiatives of the Board. We also thank the members of our Board who have always been a significant part of all our endeavours.

We also wish to express our sincere appreciation for CA. Arti Bansal, Secretary, Board of Internal Audit and Management Accounting, ICAI, and her team for their efforts in giving final shape to the publication.

We are sure that this publication would prove to be a useful reference Guide for our members and others concerned to discuss the changes envisaged by the revised RBI guidelines and analyse implications, so that concurrent auditors can perform their audits effectively and efficiently.

We will be glad to receive your valuable feedback at biana@icai.in. We also request you to visit our website <https://internalaudit.icai.org/> and share your suggestions and inputs, if any, on internal audit and Management Accounting.

CA. Rajendra Kumar P
Chairman
Board of Internal Audit &
Management Accounting

CA. Charanjot Singh Nanda
Vice-Chairman
Board of Internal Audit &
Management Accounting

September 4, 2023

New Delhi

Foreword to the Second Edition

For a growing and dynamic economy like India, that aspires to be globally competitive, a sound and inclusive banking system is extremely important. The stability of various segments in the economy particularly of the financial sectors is directly or indirectly dependent on the banking sector. Indian banks have modernized their processes, restructured their organisations into business verticals, completed Core Banking Solution implementation and launched several products in both the retail and wholesale banking segments to keep pace with the growing challenges.

This changing landscape and the emphasis on risk management and control function makes the role of concurrent auditors very critical. RBI has revised its 1996 concurrent audit guidelines and issued “Concurrent Audit System in Commercial Banks – Revision of RBI’s Guidelines” in July, 2015. These guidelines focus on effective controls, importance of checking high risk transactions and coverage of fraud prone areas. In the light of these new Guidelines, the Internal Audit Standards Board (IASB) of the Institute has thoroughly revised “Manual on Concurrent Audit of Banks (2012 edition)”, including the impact of various applicable new/ revised RBI Circulars issued during the period.

I congratulate CA. Mukesh Singh Kushwah, Chairman, CA. Anil S. Bhandari, Vice-Chairman and other members of the Internal Audit Standards Board on issuance of this revised Manual.

I am sure that this revised edition would help the members in discharging their responsibility, as concurrent auditors, in an efficient and effective manner.

September, 9, 2016
New Delhi

CA. M Devaraja Reddy
President, ICAI

Preface to the Second Edition

Technological innovation, asset quality, capital adequacy, financial inclusion and talent management are some of the key issues facing the Indian banking industry. Banks are facing challenges related to implementation of Core Banking Solutions, compliance with Basel norms, Non-Performing Asset (NPA) management and above all dealing with the ever-growing volume and complexity of transactions. These challenges make the role of chartered accountants crucial as they are instrumental in helping the banks to maintain reliability of different processes and timely reporting of lapses and irregularities.

Concurrent audit is essentially a management process integral to the establishment of sound internal accounting functions and effective controls and setting the tone for a vigilance internal audit to preclude the incidence of serious errors and fraudulent manipulations. Reserve Bank of India had issued concurrent audit guidelines in 1996. Since then a number of developments have taken place in banking sector and consequently RBI has issued revised Concurrent Audit Guidelines in July, 2015. Keeping this in view, the Internal Audit Standards Board has thoroughly revised “Manual on Concurrent Audit of Banks” which had been issued in 2012. Apart from taking impact of abovementioned circular and all other related new circulars/directions issued by the RBI, the revised Manual also, includes thoroughly updated Checklist for Concurrent Audit. This revised edition includes new chapters on important areas like, Treasury, Forex and Core Banking Solutions. For ready reference, text of all important Master Circulars and Master Directions issued by the RBI, impacting concurrent audit, have been included in the CD. However, it is extremely important that the concurrent auditors should keep themselves updated regarding all relevant internal guidelines/circulars/important references as well as relevant circulars/directions being issued by the RBI from time to time.

At this juncture, I wish to place on record my sincere thanks to all the members of the Study Group formed under my convenorship at Delhi, viz., CA. Rakesh Garg (co-convenor), CA. Sanjay Gupta, CA. Naresh Gupta, CA. Anil Aggarwal, CA. Anu Pandey, CA. Sandeep Goel, CA. Yogesh Malik and CA. Kapil Chatwal for taking time out of their pressing preoccupations and comprehensively revising and updating this Manual. I would also like to

express my gratitude to CA. Shrinivas Y. Joshi, Shri Govadda Subba Rao, Shri P. T. S. Murthy, CA. Kuntal P. Shah, CA. Sachin Ambekar, CA. Tushar Kanti Basu, CA. Anagha Thatte, CA. Vinod Karandikar, CA. Sanjay V. Shah, CA. Dhananjay J. Gokhale, Shri V. Somasekhar, CA. Ramesh A. Shetty and CA. S. Dhayanidhi for providing important support to the group.

The Study Group members were deeply concerned with the expanded scope of work of concurrent audit which may not so strictly fall within the ambit of concurrent audit, and also the remuneration which is not commensurate with the workload of concurrent auditors. Further, it was felt that for good governance and effective implementation of RBI Circulars, the banks should adopt uniform reporting format for concurrent audit and also review requirement of compulsory attendance by certain banks.

I would also like to thank to CA. M. Devaraja Reddy, President, ICAI and CA. Nilesh Shivji Vikamsey, Vice President, ICAI for their continuous support and encouragement to the initiatives of the Board. I must also thank my colleagues from the Council at the Internal Audit Standards Board, viz., CA. Anil Satyanarayan Bhandari, Vice- Chairman, IASB, CA. Tarun Jamnadas Ghia, CA. Mangesh Pandurang Kinare, CA. Dhinal Ashvinbhai Shah, CA. Babu Abraham Kallivayalil, CA. K. Sripriya, CA. M. P. Vijay Kumar, CA. Ranjeet Kumar Agarwal, CA. Sushil Kumar Goyal, CA. Debashis Mitra, CA. Shyam Lal Agarwal, CA. Kemisha Soni, CA. Sanjiv Kumar Chaudhary, CA. Sanjay Vasudeva and Shri Vithayathil Kurian for their vision and support. I also wish to place on record my gratitude for the co-opted members on the Board viz., CA. Anil Kumar Jain, CA. Kartik Bhaskarkumar Radia, CA. Krishna Kumar T., CA. Vipin Gupta, CA. Vishwanath K., CA. Yashwant Jaywant Kasar and special invitee viz., CA. Shobhit Dwivedi for their invaluable guidance as also their dedication and support to the various initiatives of the Board. I also wish to express my sincere appreciation for CA. Jyoti Singh, Secretary, IASB and her team for their efforts in revising this Manual.

I am sure that the members and other interested readers would find this revised Manual immensely useful.

October 13, 2016
New Delhi

CA. Mukesh Singh Kushwah
Chairman
Internal Audit Standards Board

Foreword to the First Edition

With financial sector reforms along with information and communication technology revolutions, the operational environment of the banks has changed very fast. While deregulation has opened up opportunities for banks to diversify into new areas like Investment Banking, Gold Banking, Mortgage Financing, Depository Services and Securitization, E-Banking etc., liberalization is opening up the grass for new players, which is increasing competition among all the banks. Key words that describe the change are operational flexibility and functional autonomy, which has bestowed greater freedom to banks to take on competition. More stress is being laid on operational efficiency and prudent risk management.

The concurrent audit system has become very crucial and important for banks. It is regarded as part of a system to ensure timely detection of irregularities and lapses, which helps in minimization of the irregularities and fraudulent transactions at branches. The concurrent auditors must be fully abreast with the changes in functioning and operational activities of the banks.

I am happy to note that the Internal Audit Standards Board is bringing out this Manual on Concurrent Audit of Banks for the Guidance of the members and banks' management. I congratulate CA. Abhijit Bandyopadhyay, Chairman, Internal Audit Standards Board and other Board members on the issuance of this Manual.

I am sure that this Manual will assist the concurrent auditors to perform the tasks and to enhance the quality of work assigned to them. I am sure that the Board will continue to bring such more publications for the benefit of members.

17th November, 2008
New Delhi

CA. Ved Jain
President, ICAI

Preface to the First Edition

The banking industry is the quintessential lubricant of the wheel of economic growth. Best of industrial growth policies for giving impetus to economic growth would fall flat if the banking industry is unable to provide the support and facilities required to the entrepreneurs who ultimately implement those policies at the micro level. Further, being the one who handles and manages the hard-earned funds of the public, the banking industry has an equally proactive role to play in creating and sustaining the trust of the common man therein. The slightest breach in this trust can lead to severest of consequences on the economic as well social growth of a nation. With its reputation risk running extremely high, a bank cannot, therefore, afford to function in a manner other than that which generates goodwill among the public at large. This in turn culminates into a bigger responsibility for a regulator like the Reserve Bank of India to ensure effective and efficient functioning of the banks in the country.

The system of concurrent audit in banks was, accordingly, introduced by the Reserve Bank of India in 1992 pursuant to the recommendations of the Ghosh Committee. The main objective of the system is to ensure compliance with the audit systems in banks as per the guidelines of the Reserve Bank of India and importantly, to ensure timely detection of lapses/ irregularities. In view of their core competence in the area of finance and accounting, risk management, understanding of the internal functioning and controls of banks, etc., the banking sector has been relying extensively on them to comply with these requirements of the regulator.

The Institute at its end has been extending a helping hand in the form of training programmes/ seminars and reading literature in the relevant area to its members to help them effectively discharge the onerous responsibilities placed on them. This Manual on Concurrent Audit of Banks being brought out by the Internal Audit Standards Board of the Institute is, I personally feel, a landmark in this direction. Written by a panel of auditing experts drawn from the banking sector, the Manual is a comprehensive, self-contained document in itself, touching upon almost all critical aspects in concurrent audit of banks. It is divided in four main parts, viz., understanding of the banking business and the legal framework, domain of concurrent audit, various other assignments, model manual of instructions. For easy understanding and

practical implementation, the Manual contains a variety of checklists and is written in a very lucid and logically flowing manner.

At this juncture, I wish to express my sincere gratitude to CA. Partha Sarathi De, CA. S.C. Basu, CA. Gorachand Mukherjee, CA. Subrata Das, CA. Asit Adak, CA. Pradip Majumdar and CA. Dilip Basu for sparing time out of their professional and personal preoccupations and sharing wealth of their experience in the area of concurrent audit in the form of this Manual. I am also obliged to CA. Ved Kumar Jain, President and CA. Uttam Prakash Agarwal, Vice President for their unstinted support and encouragement to the activities of the Internal Audit Standards Board. I also wish to thank my colleagues in the Internal Audit Standards Board and the Secretariat for their invaluable guidance and support in giving final shape to this Manual.

I firmly believe that this publication would serve as a basic guide for the members and other readers interested in the subject.

10th November, 2008
Kolkata

CA. Abhijit Bandyopadhyay
Chairman,
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PART I

Understanding the Banking Business and Its Legal Framework

Chapter 1

Banking System in India

Types of Banking Institutions in India

The following types of Banking Institutions Prevail in India:

- (a) Commercial Banks
- (b) Regional Rural Banks
- (c) Co-operative Banks
- (d) Development Banks – Term Lending Institutions
- (e) Payment Banks
- (f) Small Finance Banks
- (g) Branches of Foreign Banks

Commercial Banks

Commercial Banks in India are classified as:

- (a) Public Sector Banks
- (b) Private Sector Banks
- (c) Foreign Banks

All types of Banks are under the overall Control and supervision of RBI, irrespective of Ownership.

Public Sector Banks

1. Public Sector Banks are categorised as follows:
 - (a) State Bank of India (SBI)
 - (b) Nationalised Banks
2. Associate Banks of SBI were State Bank of Bikaner and Jaipur, State Bank of Hyderabad, State Bank of Mysore, State Bank of Patiala and State Bank of Travancore. Now all the above said associate banks have been merged with SBI and all those Associate Banks are now called as “State Bank of India”.

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3. Government of India has nationalised 14 banks in the year 1969 and another 6 Banks in the year 1980. Certain nationalised banks were later merged.
4. Majority Share capital of Commercial Banks is owned by Government and few share capital are allotted to Private individuals/ institutional shareholders in India.

Private Sector Banks

1. The ownership of Private Sector Banks is with institutional shareholders, individuals and body corporate.
2. The Private sector banks are also funding Priority sector advances as per the provisions of Banking Regulation Act.
3. Private Sector Banks are of the following types:
 - (a) Indian Scheduled Commercial Banks other than Public Sector Banks (Existing Old Private sector banks and new generation Private Banks were granted licences by RBI in March 2014).
 - The Term 'Scheduled Commercial Banks' refers to commercial banks which are included in the Second Schedule to the Reserve Bank of India Act, 1934.
 - Under Section 2(e) of the RBI Act, a scheduled Bank is conferred two main privileges (a) availing of refinance from RBI and/ (b) permission to participate in the call/ notice money market.
 - It may be noted that all scheduled banks are not commercial banks.
 - Some Cooperative banks are also scheduled banks.
 - Banks in India are set up under the specific act or registered under the companies/ co-operatives act.
 - (b) Non- Scheduled Banks.
 - (c) Indian Branches of Banks incorporated outside India, commonly referred to as 'Foreign Banks'.

Banks set own subsidiaries - Wholly owned or Partly Owned

- (a) In the following areas, Banks have set up their own subsidiaries to carry out some specialised spheres of activity:
- Merchant Banking
 - Funds Management
 - Housing Finance
 - Primary dealership
 - Pension Fund Management
 - Insurance Business
 - Stock Broking
 - Credit Card Activity
 - Factoring
- (b) These subsidiaries do not carry on all the principal functions of a commercial Bank.

Regional Rural Banks (RRBs)

1. These Banks have been established with a view to develop the rural economy by providing, for the purpose of development of agriculture, trade, commerce, industry and other productive activities in the rural areas, credit and other facilities, particularly to the small and marginal farmers, agricultural labourers and artisans and small entrepreneurs.
2. RRB is legally permitted to engage any Banking business.
3. Regional Rural Banks Act 1976 governs the functions of RRB.
4. Section 18 of RRB Act 1976 list the following businesses which such a bank may undertake:
 - (a) The granting of loans and advances, particularly, to small and marginal farmers and agricultural labourers, whether, individually, or in groups and to cooperative societies, including agricultural marketing societies, agricultural processing societies, co-operative farming societies, primary agricultural credit societies or farmer's service societies, for agricultural purposes or agricultural operations or for other purposes connected therewith.

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- (b) The granting of loans and advances, particularly artisans, small entrepreneurs and persons of small means engaged in trade, commerce or industry or other productive activities, within the notified area in relation to the RRB.
- 5. RRB is also covered by all the provisions of SARFAESI Act, 2002.
- 6. Now Central Government and RBI have taken special measures to strengthen RRB and allowed to the following additional banking transactions.
 - (a.) Lend to non-target group in addition to weaker sections.
 - (b.) Issuance of Bank Guarantee/ Demand Draft/ Travellers Cheques, etc.
 - (c.) RRB is also allowed to do banking transactions beyond its permitted local limits, i.e., it can also do the business outside the limits permitted.
- 7. In the wake of the developments, as stated in the Para 6, the distinction between commercial banks and RRBs has become somewhat blurred.
- 8. RRB has a Public Sector Bank as its 'sponsor bank'.
- 9. Sponsor Bank of RRB is also required train personnel of RRB as also to provide managerial and financial assistance to such bank during the First 5 years of the RRB functioning. This period can be extended by Central Government, if needed.
- 10. RRB is also allowed to function under the overall supervision and control of RBI.
- 12. The RRB's are regulated by the RBI and supervised by NABARD.

All the RRBs are subject to all kinds of Audit such as Statutory Audit, Revenue Audit, Concurrent Audit, etc., as per RBI norms.

Co-operative Banks

- 1. The Co-operative Banks come under the respective State Governments' Co-operative Societies Act.
- 2. The following are the types of Co-operative Banks:
 - a) Urban Co-operative Banks
 - b) State Co-operative Banks
 - c) District Central Co-operative Banks

d) Land Development Co-operative Banks

3. These are the banks in the co-operative sector which cater primarily to the credit needs of the farming and allied sectors. Mainly these banks concentrate on agriculture and weaker sections.
4. Respective State Governments and Public contribute towards Share capital of the Cooperative Banks.
5. For Rural Level, Agriculture and allied finance is arranged with 3 tier structure of Cooperative banks and societies in each and every State:
 - (a) At the State Level - State Cooperative Apex Bank.
 - (b) At the District Level – Each district has Central Cooperative Bank named after the district.
 - (c) At the Village Level – Primary Cooperative Credit Society or Rural Bank catering to the needs of the villagers.
6. Every cooperative Banks including cooperative societies are having their own By Laws for management.
7. While Incorporation/ Registration and management related activities are regulated in the States by the Registrar of Cooperative Societies or the Central Registrar of Cooperative Societies (for multi-State cooperative Banks).

Foreign Banks

1. Foreign Banks operate in India through a Network of branches and do not have a separate legal entity existence in India.
2. RBI regulates the functioning of these banks in India, with regard to scale and nature of business they undertake in India.
3. The consent of RBI is required to process the Data out of the country by theses foreign banks.

Payment Banks

1. Since 2014, Payment Banks have been introduced in the Indian Financial System.
2. The basic objectives of these banks are two:

- (a) Providing Small Savings Account.
 - (b) Payments/remittance services to migrant labour workforce, low-income households, small businesses, other unorganized sector entities and other users.
 - (c) Their scope of activities includes the acceptance of deposits, presently restricted to holding a maximum balance of Rs. Two lakh per individual Customer, issuance of ATM/Debit cards but not Credit cards, payments and remittance services through various channels, acting as Business Correspondents (BC) of another bank and distribution of non-risk sharing simple financial products like Mutual Fund Units and insurance products, etc.
 - (d) No lending activities are permitted in Payment Banks.
3. Payment Bank is regulated by Reserve Bank of India.

Small Finance Banks (SFB)

1. In November 2014, SFBs have been introduced in the Indian Financial System.
2. Two Basic objectives are as follows:
 - (a) Provision of vehicle savings.
 - (b) Supply of credit to small business units; small and marginal farmers; micro and small industries; and other unorganized sector entities, through high technology-low-cost operations.
3. Their scope of activities primarily includes undertaking basic banking activities of acceptance of deposits and lending to unserved and under-served sections including small business units, small and marginal farmers, micro and small industries and unorganized sector entities.
4. There are no restrictions in the area of operations of these banks.
5. SFBs are subject to all prudential norms and regulations of RBI applicable to existing commercial banks including maintaining CRR and SLR.
6. No forbearance has been provided for complying with the statutory provisions.
7. These banks are required to extend 75% of their Adjusted Net Bank

Credit to the sectors eligible for classification such as Priority Sector Lending by RBI.

8. Also at least 50% of their loan portfolio should constitute loans and advances up to Rs. 25 Lakhs.

Now all the SFBs are subject to Statutory Audits, Concurrent audits, Stock audits, Revenue audit, etc.

Note: The article “Perspectives on the History of the Reserve Bank of India” available on link: https://rbi.org.in/scripts/BS_ViewBulletin.aspx?Id=21930 takes a bird's eye view of the history of the Reserve Bank of India and unravels the treasure trove embodied therein. Spanning over five volumes, the Reserve Bank's history is an insightful account of its policies, operations and institutional evolution. During the journey, its public policy initiatives and institutional, structural and financial reforms transformed the Indian economy. It is not only an institutional history of India's central bank, but also a major part of India's economic and financial history. Presented in a lucid, interesting and analytical way, it is a precious repository of knowledge for everyone.

Chapter 2

Banking Products and Services

Major Products and Services Provided / Rendered by Commercial Banks

Acceptance of Deposit

1. As per Section 5(b) of Banking Regulation Act, 1949, “banking” means the accepting the deposits of money from the public for the purpose of lending or investment.
2. The deposits are repayable on demand or otherwise, and withdrawal by cheque, draft, order or otherwise.
3. Acceptance of Deposits from the public is one of the most important functions of a Commercial Banks.
4. The following are the various kinds of deposits that are accepted by Commercial banks:
 - (a) Term Deposits
 - (b) Savings Bank Deposits
 - (c) Current Account Deposits
 - (d) Recurring Deposits
 - (e) Savings cum Term Deposits
 - (f) Various other innovative deposit products
5. There are “no ceilings” (minimum and maximum) of deposits can be accepted by the Banks.
6. Banks pay only Fixed (Simple and Cumulative) interest on deposits, i.e., bank interest rates applicable on the date of money deposited.
7. Premature withdrawal of Deposits, subject to Bank’s policy for penalty is allowed.
8. Payment of interest is an Outflow and is a revenue expenditure for the bank.

Granting of Advances

1. It is one of most important functions of all kinds of Banks in India.
2. The following are the few types of Advances that are granted by Banks in India:
 - (a) Term Loan
 - (b) Cash Credit Loan
 - (c) Overdraft Loan
 - (d) Agricultural Loan
 - (e) Purchase or Discount of Bills
 - (f) Issue of Bank Guarantee (Non-Funded Loans)
 - (g) Issue of Letter of Credit (Non-Funded Loans)
 - (h) Issuance of Commercial Papers
 - (i) External Commercial Bank Loans on behalf of Bank/Borrower
 - (j) Securitisation of Receivables
3. The details of these loans are discussed in another Chapter in this Manual.

Remittances

1. This involves transfer of funds from one place to another.
2. The following are the common Modes of Fund Transfer:
 - (a) Draft
 - (b) Electronic Fund Transfer – RTGS/NEFT/IMPS/UPI/ECS
3. Highlights of Demand Draft:
 - (a) It is issued by One Branch of the Bank to be payable at the other branch of the same bank, on the request of the Bank Customer.
 - (b) In case, there is no Branch for the Bank is available at the place of destination, the branch of another Bank with which the issuing Bank has entered into necessary arrangement.
 - (c) The Drafts are handed over to the Applicant Customer.

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4. Highlights of Electronic Fund Transfer (EFT):
 - (a) In the case of EFT, as the name suggests the funds are transferred electronically between Two banks.
 - (b) The following are the Common Mode of EFT:
 - Real Time Gross Settlement (RTGS) – which can be used for remittances of amount of Rs. Two Lakhs or above.
 - National Electronic Funds Transfer (NEFT) – which can be used to transfer any amount.
 - Immediate Payment Service (IMPS).
 - Unified Payment Interface (UPI)
 - Electronic Clearing System (ECS)

Collections

1. The customers can lodge various instruments of the following for the collection of the amount drawn in favour of them from the drawee (the bank or the drawer of the Bill):
 - (a) Cheques
 - (b) Demand Drafts
 - (c) Pay orders
 - (d) Travellers Cheques
 - (e) Dividend and interest warrants
2. They can also lodge their term deposit receipts and other similar instruments with the Bank for Collection of the proceeds from the Bank with which the term deposit is maintained.
3. Banks also collect instruments issued by Post Offices, like National Savings Certificate, Postal Orders, etc.
4. Banks also credit Tax Refund Orders issued by the Tax Departments to the accounts of their customers. The Instruments such as Cheques, Demand Draft are collected through Continuous Cheque Truncation System (CCTS). Cheque Truncation System (CTS) was pioneered by RBI for faster clearing of cheques. It is implemented since 01.08.2013. It involves sending an Electronic Image of the Cheque together with

Magnetic Ink Character Recognition (MICR) Data and other relevant fields like Date of presentation, presenting bank names etc. This procedure eliminates the need for physical transfer of cheques across branches, except in certain cases. CTS ensures faster Clearing, lesser chances of frauds with no fear of loss of cheque in transit. Highlights of Clearing House:

- (a) The Clearing House in India is managed by RBI, SBI or any other Bank nominated by RBI.
- (b) Clearing House helps to settle the claims of various Banks against each other by way of making book entries in their accounts in the form “to/by”, so that the transactions between the banks have been settled easily.
- (c) Clearing House settles the inter-Bank transactions among the Local Participating member Banks.
- (d) Post Office has also become Participating Member of the Bank in the Clearing House.
- (e) In case a Bank has many branches within the area of clearing House, it nominates one Branch to act as the ‘Nodal Branch’ of that Bank for all the branches within that areal.
- (f) This nodal branch collects instruments to be presented to other branches also.
- (g) The accounts of all member banks are maintained by the clearing house.
- (h) All Member banks have to pay an agreed sum to the bank managing the clearing house for meeting the cost of infrastructure and services it provides to them.

5. In addition to the regular clearing houses as discussed above, Electronic Clearing Service (ECS) is also in vogue. ECS takes two forms:

ECS Credit:

- (a) There is a single receiver of funds from a large number of customers, e.g. Public Utilities, Mutual Funds, etc.

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- (b) The Beneficiary (i.e. the receiver of funds) obtains mandate from its customers to withdraw funds from their specified Bank accounts on a Particular Date.
- (c) These customers may have accounts with different Banks in the same clearing house area.
- (d) Before the specified date, the beneficiary complies Bank-branch-wise particulars of the accounts to be debited and furnishes the details in the electronic media to its own Bank which in turn arranges to provide them to the banks concerned through the clearing house, for verification of particulars of accounts.
- (e) Any discrepancies are rectified, and on the specified date, the accounts are debited by the respective banks and the beneficiary get the credit.

ECS Debit:

- (a) There is a single account to be debited against which a number of accounts with a number of banks in the same clearing house area are credited.
 - (b) This system is useful for distribution of dividend/interest, payment of salaries by large units, etc.
6. Roll out Speed Clearing is one of the many initiatives taken by RBI for improving efficiency in the time frame and process of collection of cheques through CCTS.

Receipt of Foreign Contribution on Behalf of the Registered Persons/ Organisation

1. With effect from July 1, 2021, all the FCRA NGO should compulsorily open account with State Bank of India, Main Branch, New Delhi for initial remittance/ receipt of foreign contribution. Thereafter the same can be transferred to the respective banks of the registered persons/ organisation in separate account.
2. Banks need to ensure that the concerned persons/ organisation are registered with the Foreign Contribution Regulation Act to receive such foreign contribution if required by law, and that no branch other than the specified branch accepts 'foreign contribution'.

Cash Management Product

1. It is a derivative of the collection business; this facility is provided for expeditious transfer of funds collected by the customer at the specified centre in the country to his central account through core banking system.
2. It is particularly useful for large units which have their sales/ collection network in a very wide geographical area.
3. Only selected branches of a bank may handle the business due to the infrastructural requirements.

Issuance of Letters of Credit and Guarantees

1. For the customers engaged in business, industrial and commercial activities, issue of Letter of credit and Bank guarantee are two important services rendered by Banks.
2. Letter of Credit (LC) is an undertaking by a bank to the payee (the supplier of goods and/ or services) to pay to him, on behalf of the applicant (the buyer) any amount up to the limit specified in the LC, provided the terms and conditions mentioned in LC are complied with.
3. Guarantees are required by the customer of banks for submission to the buyers of their goods/services to guarantee the performance of contractual obligations undertaken by them or satisfactory performance of goods supplied by them or for submission to certain departments, like Excise and customs, GST, Electricity Boards or to suppliers of goods etc in lieu of the stipulated security deposit.

Merchant Banking Business

Many banks render Undertaking Services for IPO. The customer and the bank must agree to the modalities of the scheme, like names of branches authorised as collecting branches, the procedure for retaining the subscription and its remittance periodically the documents required by the customer from the collecting branches, etc.

Credit Cards

1. The processing of applications for issuance of credit cards is usually entrusted to a separate division at the central office of a bank.

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2. The dues against the credit cards are collected by specified branches.
3. Many of them also act as 'cash points' to provide cash to the cardholder on demand up to the specified limits.
4. Most credit cards issued by banks are linked to one of credit card networks like RUPAY, VISA, Master Card or Amex.
5. "Spiralling debt" is the predominant risk of using a credit card.
6. Normally customers who are using the Credit cards are not paying their balance in full every month. The bank charges interest on the outstanding balance on the credit card.

Technology Based Services

1. Internet Banking Services and Mobile Banking services are the need of the Hour and most of the banks have started to offer these services to their customers.
2. Some banks, acting as stockbrokers, also provide facility to their customers to buy or sell securities on stock exchanges through the internet.
3. The fast-changing technology has synchronised banking facility in such a way that the customer need not physically visit the bank. The banks are now providing the facility of payment of utility bills, railway reservation, and tax deposition through ATM/Internet Banking and are also providing value added services like recharge facility to mobile phone users.

Dividend Interest/ Refund Warrants

1. Many entities require facilities for distribution of funds to their shareholders and others. For this purpose, they issue warrants in favour of shareholders/ others payable at the designated branches of specified banks, with a prior arrangement with the banks concerned.
2. The aggregate amount of the warrants or other instruments issued is deposited by the entity with a nodal branch.
3. The designated branches Credit the amount of dividend/ interest to the account of the individual customer.

Safe-Keeping Services

Banking Products and Services

1. Banks provide services for safe keeping of the scrips and valuables of customers in their vaults.
2. A receipt is issued to the customer by the branch at the time of deposit of the items and an acknowledgement is obtained from him at the time of delivery.
3. Each transaction – a receipt or delivery – is duly recorded in appropriate register(s) and periodically, the items physically available are cross checked with the balances as per registers.

Lockers

1. This facility is provided to customers for safe keeping their valuables, in lockers.
2. Specially designed lockers are purchased from reputed manufacturers by bankers, and these are kept at specially built strong rooms at branches.
3. These lockers are let out on hire to the Branch customers and the rental charges have been recovered based on the “size” of the lockers.
4. The branch has no knowledge of the contents of the locker.
5. Only the account holder(hirer) or his representative, duly authorised by the account holder, can operate the locker.
6. Each access to the locker is properly recorded in the appropriate registers.

The new regulations of Lockers effective from December 2023, clearly define what can be stored (jewellery and documents) and what cannot be stored in lockers (such as cash, drugs, perishable items, arms and others).

Handling Government Business:

1. Banks act as agents of RBI for receipts and payments on behalf of government departments like income tax, GST, etc.
2. There are authorised branches to handle the specified type of work.
3. Normally, a specified branch acts as a Nodal Branch for a particular segment of the government business within a given geographical area. The responsibility of the Nodal branch includes obtaining details of

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transactions from the linked branches and to reconcile their accounts *inter se* and with the department concerned.

4. Banks are remunerated for handling this business by way of service charges which are usually as agreed or a stated percentage of the collections or payments, as the case may be.

Depository Participants (DP) Services

1. The Depository system is meant to facilitate quick transfer of stock market securities in a Dematerialised form from the seller to the buyer by using satellite connectivity.
2. The Depository Scheme is operated presently by two Depositories:
 - (a) Central Depository Services Limited (CDSL)
 - (b) National Securities Depository Limited (NSDL)
3. Depository participants i.e. bank branches providing depository services are in effect agents of the depository concerned.
4. Each participating branch has to get itself registered with a depository.
5. The customer must open an account with the branch which provides DP services. This account is debited by the branch with the securities sold by the account holder and credited with the purchases.

Automated Teller Machine (ATM)

1. Operations on ATMs are through a card (popularly known as ATM card) which contains information about the cardholder in a magnetic form.
2. The cardholder has to also use the password (also known as Personal Identification Number i.e. PIN) to carry out any transactions through ATM.
3. Earlier ATMs were merely used as cash dispensing machines but now-a-days other services like, deposit of cash and instruments, balance enquiry, etc. are also being provided by many banks.
4. ATMs may be on-site (housed in the branch premises) or off-site.
5. The transactions routed by the customers through the ATMs may be entered into the books of account of the branch either on-line (i.e.,

simultaneously with the transactions) or off-line. However, on an off-line mode, the proper recording of transactions needs to be ensured.

Exchange of Notes

1. Banks exchange mutilated currency notes from the public for good quality notes.
2. These mutilated currency notes are periodically sent to RBI which gives equivalent credit to the branch concerned.
3. Damaged, soiled or missing numbers in any currency Notes (Rupee) can be deposited at any public sector bank branches or RBI office without any forms being filled out.
4. At a time, maximum of 20 currency notes can be exchanged and whose maximum value should not exceed Rs 5000. For a greater number of notes or value exceeding Rs 5000/- the banks may accept them against receipt, but the value will be credited later.
5. The banks also act as agent of the RBI at the time of exchange of currency notes at the time of demonetisation of specified currency notes.

Debit Cards

1. Debit cards are issued by bank which are linked to the account of the customer.
2. The debit cards are generally issued from Central office of the bank.
3. The Debit Card facilitates the customer to pay at any authorised outlet as well as withdraw money from ATM from his account.
4. The Debit cards are sometimes networked with inter-bank network.

Auto Sweep Facility in Savings Account

The banks are offering auto sweep facility in saving accounts of their customers where balance exceeding a certain limit automatically gets transferred to term deposit account having higher rate of interest and in case of need, the funds in term deposit automatically get transferred to saving account.

Third Party Advertisement on ATM Network

The banks are providing advertisement facility to the vendors on ATM Network. The advertisement on ATM Network provides the opportunity of earning revenue to the Bank.

Derivatives

Banks offer a variety of derivative services to manage risk, hedge against fluctuations in underlying assets, and potentially generate profits from price changes. These services typically include forward contracts, futures contracts, options contracts, and swap contracts. Derivatives are financial instruments whose value is derived from the price of an underlying asset, such as stocks, bonds, commodities, currencies, or interest rates.

Prepaid Payment Instruments (PPI) in India

1. The Main objective of this PPI is to get access to the amount already paid into the account.
2. Without any physical exchange of card or cash, one can purchase the required goods.
3. Examples of Prepaid Payment Instruments are Smart Cards, Online accounts, Online Wallets, Magnetic Strip Cards, Paper Vouchers, Mobile Wallets and any such instrument which can be used to access the PPI.
4. There are two types of PPI:
 - (a) Small PPIs
 - (b) Full KYC PPIs
5. Banking Institutions or Non-Banking Institutions authorised by RBI are eligible to issue PPI. Without getting authorisation from RBI PPI cannot be issued by anyone.
6. The PPI that can be issued in the country are classified under Three categories:
 - (a) Closed System PPI
 - (b) Semi Closed System PPI
 - (c) Open System PPI

7. In the process of moving from cash-based payments to electronic payments to achieve the vision of less- cash society, a new category of semi- closed prepaid payment instrument is being introduced with certain features which is named as PPI for mass transit system (PPI-MTS) vide RBI latest master circular DPSS. CO. PD No. 2/02 14-006/2015-2016 dated 01.07.2015 on issuance and operation of prepaid instrument in India.
8. "Issuer" may be the persons operating the payment systems issuing prepaid payment instruments to individuals/organizations. The money collected is used by these people to make payment to the merchants who are part of the acceptance arrangement directly, or through a settlement arrangement. Further, it requires that other non-bank persons issuing PPI are needed to maintain their outstanding balance in an escrow account with any scheduled commercial bank subject to the following conditions:
 - (a) The amount so maintained be used only for making payments to the participating merchant establishments.
 - (b) No interest is payable by the bank on such balances.
 - (c) A quarterly certificate from the auditors be submitted certifying that the entity has been maintaining adequate balance in the account to cover the outstanding volume of payment instruments issued.
 - (d) The entity shall also submit an annual certificate, as above, coinciding with the accounting year of the entity to the Reserve Bank of India.
 - (e) Adequate records indicating the daily position of the value of instruments outstanding vis-à-vis balances maintained with the banks in the escrow accounts be made available for scrutiny to the Reserve Bank or the bank where the account is maintained on demand.
9. Please Ref: Master Directions on PPI (Updated on 27/12/2024) in RBI/DPSS/2021-22/82 CO. DPSS.POLC.No.S479/02.14.006/2021022.
10. Unified Payments Interface (UPI) is an instant payment system developed by National Payments Corporation of India (NPCI) in 2016. It is used on mobile devices to instantly transfer funds between two bank accounts. Most of the scheduled banks provide these services to their

customers. With the exponential growth of UPI, India has become the world's largest real time payment market.

Para-banking Activities

1. Banks also undertake certain eligible financial Services or para- banking activities departmentally. Some of these are as follows:
 - a) Bank may act as a broker departmentally subject to the conditions mentioned under Section 18 (d) of the Master Direction) **(Financial Services provided by Banks) Directions, 2016 (Updated as on August 10, 2021)** on Insurance agency business.
 - b) Corporate Agency of Insurance Companies can be undertaken departmentally by banks provided there is a board approved policy in place detailing the products and the manner in which they can be distributed. The policy should be in conformity with extant RBI and other regulatory guidelines.
 - c) Banks may undertake to outsource certain eligible financial services or para banking activities as per the instructions issued by the RBI to banks for undertaking various financial services as stated in 'Master Direction in compliance with RBI guidelines No. RBI/2006/167/DBOD.NO. BP>40/21.04.158/2006-07 dt November 3, 2006, on Managing Risks and Code of Conduct in Outsourcing of Financial Services by banks can set up subsidiary for undertaking such activities only with prior approval of RBI. Some of those activities are given below:
 - (a) *Equipment Leasing, Hire Purchase and Factoring Services*: Banks may invest in other equipment leasing/hire purchase/factoring companies within the limits specified in Section 19 (2) of Banking Regulation Act 1949 with prior approval of the RBI, but they shall not act as promoters of such companies.
 - (b) *Mutual fund business*: Banks are not permitted to directly undertake mutual fund business but sponsor mutual funds, subject to the RBI guidelines in this regard. Banks normally refer clients to these mutual funds and earn a commission in return. Banks may enter into agreement with mutual funds for marketing, the mutual fund units subject to the terms and conditions specified in the RBI master circular on "Para Banking Activities".
 - (c) *Money Market Mutual Funds (MMMFs)*: Banks can also sponsor

MMMFs business subject to the prior approval of the RBI. The MMMFs are, however, subject to regulation by the Securities and Exchange Board of India. Banks also, at time, provide cheque writing facilities for MMMFs subject to the RBI guidelines in this regard.

- (d) *Entry of banks into Insurance Business*: Banks intending to set up insurance joint ventures with equity contribution on risk participation basis or making investments in the insurance companies for providing infrastructure and services support should obtain prior approval of Reserve Bank of India before engaging in such business. However, insurance business will not be permitted to be undertaken departmentally by the banks.
- (e) *Primary Dealership Business*: Banks may undertake Primary Dealership Business through a subsidiary registered as an NBFC or departmentally subject to authorisation from RBI.
- (f) *Pension Funds Management*: Banks have been permitted to undertake Pension Funds Management (PFM) through their subsidiaries set up for the purpose subject to their satisfying the eligibility criteria prescribed by Pension Fund Regulatory and Development Authority (PFRDA) for Pension Fund Managers. PFM cannot be undertaken departmentally. Banks intending to undertake pension funds management should follow the guidelines set out in the RBI Master Circular No.DBR.NoFSD.BC.19/24.01.001/2015-16 dated July 1, 2015, on “Para - Banking Activities”.
- (g) *Portfolio Management Services*: The general powers vested in banks to operate Portfolio Management Services and similar schemes have been withdrawn vide RBI circular DBOD.No.BC.73/27.07.001/94-95 dated June 7, 1994, on Acceptance of Deposits/Funds under Portfolio Management Scheme. No bank, therefore, is permitted to, restart or introduce any new PMS or similar scheme in future without obtaining specific prior approval of the RBI. However, bank-sponsored NBFCs are allowed to offer discretionary PMS to their clients, on a case-to-case basis. The banks operating PMS or similar scheme with specific prior approval of RBI have to strictly observe the conditions given in RBI Master Circular No. DBR.No.FSD.BC.19/24.01.001/2015-16 dated July 1, 2015, on “Para Banking Activities”.

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- (h) *Referral Services*: Banks can offer referral services to their customers for financial products subject to the following conditions:
- The bank/ third party issuers of the financial products should strictly adhere to the KYC/AML guidelines in respect of the customers who are being referred to the third-party issuers of the products.
 - The bank should ensure that the selection of third-party issuers of the financial products is done in such a manner so as to take care of the reputational risks to which the bank may be exposed in dealing with the third-party issuers of the products.
 - The bank should make it explicitly clear upfront to the customer that it is purely a referral service and strictly on a non-risk participation basis.
 - The third-party issuers should adhere to the relevant regulatory guidelines applicable to them.
 - While offering referral services, the bank should strictly adhere to the relevant RBI guidelines.
- (i) *Underwriting of Corporate Shares and Debentures*: Banks can undertake underwriting of corporate shares and debentures within the ceiling prescribed for the bank's exposure to capital markets and subject to the Provisions contained in the Section 19(2) and 19(3) of the Banking Regulation Act, 1949. The guidelines contained in the SEBI (Underwriters) Rules and Regulations, 1993 and those issued from time to time are also to be complied with. Moreover, banks should not underwrite issue of Commercial Paper by any Company or Primary Dealer and not extend Revolving Underwriting Facility to short term Floating Rate Notes/Bonds or debentures issued by corporate entities. However, with effect from April 16, 2008, banks may exclude their own underwriting commitments, as also the underwriting commitments of their subsidiaries, through the book running process for the purpose of arriving at the capital market exposure both on a solo and consolidated basis.
- (j) *Underwriting of Bonds of Public Sector Undertakings*: Banks can play a useful role in relation to issue of bonds by Public Sector Undertakings (PSUs) by underwriting a part of these issues. They

may also subscribe outright initially but sell them later to the public with the aid of their wide branch network. It should, however, be ensured that the increase in the holdings of public sector bonds by banks arising out of their underwriting or subscription is kept within reasonable limits. While undertaking the underwriting of bonds of PSUs, banks should formulate their own internal guidelines as approved by their Boards of Directors on investments in and underwriting of PSU bonds, including norms to ensure that excessive investment in any single PSU is avoided and that due attention is given to the maturity structure of such investments.

- (k) *Retailing of Government Securities*: Banks are permitted to undertake the business of retailing of Government securities with non-bank clients subject to the following conditions:
- Banks are free to buy and sell Government Securities on an outright basis at prevailing market prices without any restriction on the period between sale and purchase.
 - Banks shall not undertake ready forward transactions in Government Securities with non-bank clients.
 - The retailing of Government Securities should be on the basis of ongoing market rates / yields emerging out of secondary market transactions.
 - No sale of Government Securities should be affected by banks unless they hold the securities in their portfolio either in the form of physical scraps or in the SGL Account maintained with the Reserve Bank of India.
 - Immediately on sale, the corresponding amount should be deducted by the bank from its investment account and also from its SLR assets. f) Banks should put in place adequate internal control checks/ mechanism in this regard.
 - These transactions should be subjected to concurrent audit as per RBI's extant instructions and should also be looked into by the auditors at the time of bank's statutory audit.
- (l) *Sponsors to Infrastructure Debt Funds (IDFs)*: In order to accelerate and enhance the flow of long-term funds to infrastructure projects for undertaking the Government's ambitious programme of

infrastructure development, scheduled commercial banks have been allowed to act as sponsors to Infrastructure Debt Funds (IDFs). IDFs can be set up either as Mutual Funds (MFs) or as Non-Banking Finance Companies (NBFCs). While IDF-MFs are regulated by SEBI, IDF-NBFCs are regulated by Reserve Bank of India (RBI). Banks can sponsor IDF-MFs and IDF-NBFCs with prior approval from RBI subject to the conditions given in the RBI Master Circular No. DBR.No.FSD.BC.19/24.01.001/2015-16 dated July 1, 2015, on "Para - Banking Activities".

(m) *Membership of currency derivative segment of SEBI approved Stock Exchanges:* Scheduled commercial banks (AD Category I) have been permitted to become trading / clearing members of the currency derivatives segment to be set up by the Stock Exchanges recognized by SEBI, subject to their fulfilling the following prudential requirements:

- Minimum net worth of ` Rs. 500 crores,
- Minimum CRAR of 10%
- Net NPA not exceeding 3%
- Net Profit for last 3 years

Banks which fulfil the conditions mentioned above should lay down detailed guidelines with the Board's approval for conduct of this activity and management of risks. It should be ensured that the bank's position is kept distinct from the client's position. In case of supervisory discomfort with the functioning of a bank, the Reserve Bank may impose restrictions on the bank regarding the conduct of this business as it deems fit. The banks which do not meet the above minimum prudential requirements are permitted to participate in the currency futures market only as clients.

Note: *The RBI has issued a Master Circular No.DBR.No.FSD.BC.19/24.01.001/2015-16dated July 1, 2015, on "Para-Banking Activities" containing instructions/guidelines issued by it to banks in respect of their para banking activities.*

Chapter 3

Organisational and Operational Structure of Banks

Introduction

1. Organizational structure may differ from one Bank to another.
2. Most Large Sized Banks have a Four-Tier Structure:
 - (a) Head Office
 - (b) Zonal Office
 - (c) Regional Office
 - (d) Branches
 - (e) Central Processing Centres
3. Each tier of the structure being responsible for performing the functions specified by the Head Office.
4. There are some banks having Three Tier structures without Zonal Office Concept.

Head-office Functions

At the apex level, there is the head office of the Bank whose main functions are as follows:

- Laying down policies and procedures for smooth and efficient functioning of the Bank and to review them periodically.
- Deciding on the extent of powers-financial and administrative—which may be vested in various functionaries of the Bank.
- Planning and performance budgeting.
- Asset-liability management.
- Laying down lending policy of the Bank, the risk management guidelines, and the rehabilitation and recovery guidelines including policies for compromise, settlement and write-off.

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- Deciding about the interest rates on both the deposits and the loans as well as about charges for various services and review interest rates and charges periodically.
- Treasury and investment management (usually handled by the head office, though in some cases, select large branches may also be involved in this function).
- Monitoring and controlling the functioning of various offices of the Bank. Periodic inspections and internal audit are important constituents of such monitoring and control mechanism.
- Reconciling the transactions among various offices of the Bank.
- Introducing new products and services and reviewing the existing ones.
- Issuing instructions to branches and other offices from time to time on matters deserving their attention or requiring compliance by them.
- Publish the credit policy after surveying the economic scenario of the country.
- Submission of various information to RBI and Ministry of Finance, Government of India.
- HR development function and framing of policy of development of personnel to utilize their talent.
- To obtaining various licenses for opening new branches and other financial function as per statutory rule.
- To publishing Balance Sheet and Profit and Loss statement of the Bank and organize annual general meeting of the shareholders.
- To keeping close track with the technology building and take suitable up-gradation.
- Technology Management including management of CBS and disaster management.
- Risk Management across the Bank.
- Fraud Risk Management.
- Appointment of various types of Auditors such as Central Statutory Auditor, Branch Statutory Auditor, Concurrent Auditor, etc

Zonal Office Functions

- ZO is responsible for overall working of the Bank Branches in their areas of operation.
- ZO acts as a Link between the Bank Branches and Bank Head Office, either directly or through Regional Office.
- Policies of Bank's Head office are being implemented through ZO, and everything are properly communicated to the Bank Branches.

Regional Office (RO) Functions

- RO is under the immediate control of Zonal Office.
- RO controls the Bank Branches that comes in their jurisdiction.
- All the Bank Branch requirements and needs must be taken care of Regional Office.
- RO is responsible for Business development, compliance with the laid down system and procedures, satisfactory customer service, quick redressal of complaints and submissions of the required statements/reports/returns by branches under their jurisdiction.
- RO is responsible for smooth functioning of the branches under them.
- RO organizes monthly review meeting to judge the performance of the branch under their control in all areas of operation and discuss on the internal audit and inspection report of the branch and the report of the auditor of the branch.

Branch Functions

- Branches are lowest in the hierarchy of the banking organization structure.
- In fact, the banking operations (i.e., accepting deposits and making loans) take place at the branch level.
- Their jobs are numerous, practically everything in relation to banking, except for pricing of products/services and the policy formulation.

Branch Network of Commercial Banks

1. Commercial banks are arguably the most important constituent of the banking system in India.

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2. To carry out their functions effectively, these banks have established a large network of branches in India.
3. Based on their location, these 'domestic' branches are commonly classified into rural branches, semi-urban branches, urban branches and metro branches.
4. Apart from these domestic branches, some banks have also established offices abroad.
5. The foreign offices of banks are generally of the following types:
 - (a) *Full-fledged branches* - Such branches transact all kinds of banking business.
 - (b) *Off-shore banking units* - Such branches transact foreign exchange business of any kind except domestic banking business with the residents/ corporations, etc., domiciled in the country concerned.
 - (c) *Subsidiaries* - The laws in some countries do not permit foreign banks to open their branches in those countries. Therefore, Indian banks must set up wholly or partly owned subsidiaries in such countries. Further for operational regions, commercial bank may prefer to operate through subsidiaries, if permitted, instead of opening branches.
 - (d) *Representative offices* - Such branches do not transact any banking business. The objective behind setting up such offices is to maintain close liaison with the important bodies there to promote mutual business interests.
6. Generally, branches conduct a variety of banking business under one roof. Recently, however, the trend of creating "thrust based" or "focus-based" branches is on the rise. This has led to setting up branches of banks exclusively for a specified segment of their clients.
7. Presently such specialized branches are generally of the following types (nomenclature may, however, vary from Bank to Bank):
 - (a) Personal Banking branches, catering to the needs of individual customers only.
 - (b) Commercial or Industrial Finance branches, catering to the needs of industries in the small, medium and/or large sectors.

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- (c) Recovery branches, which deal only with the recovery aspects of non- performing advances which were originally granted at other branches of the Bank.
 - (d) Housing Finance branches which deal only with housing loan proposals - from individuals, and in some cases, also from the developers of housing units.
 - (e) Agricultural Finance branches, catering to the needs of the agriculture sector only.
 - (f) Service branches, handling only the local clearing instruments received from outstation branches or from other local branches of the Bank for collection.
 - (g) Commodity specific branches, which handle the accounts, predominantly borrowable accounts, of the units belonging to a particular industry, e.g., leather, diamonds.
 - (h) Overseas or International Banking or Foreign Exchange branches catering to the banking needs of those enterprises which are engaged in imports into/exports from India.
 - (i) Corporate banking/SME/SSI branches, catering exclusively to the requirements of the large, medium and small-scale industrial units.
 - (j) NRI (Non-Resident Indian) branches, catering exclusively to the banking needs of NRIs.
 - (k) Securities branches, dealing only with the securities portfolio of the Bank.
 - (l) Branches in Gift City which are treated as international service centre (IFSC) banking units.
8. The trend towards specialization may, in future, cause the opening of dedicated branches of various other segments of clients such as, government business, remittance business, trade sector business, lockers business, rehabilitation, education loans, etc.

Central Processing Centres-

Banks may have the Central Processing Centres to process the loan applications, Customer Onboarding etc.

Role of Reserve Bank of India as the Central Bank of India

1. Banking sector in any country is controlled and regulated by Central Bank.
2. In India, the Reserve Bank of India is the Central Bank, and it controls and regulates all the functioning of all kinds of Banks in India, including Commercial Bank.
3. For all types of Banks in India, RBI is not only a Parent body, but it also acts as a guardian and controller of all those banks.
4. In India, RBI came into existence on 01.04.1935.
5. In 1949, RBI was nationalized and became a Statutory company owned by the Government.
6. RBI is responsible for development and supervision of the constituents of the Indian Financial System, which comprises Banks and Non-Banking Financial Institutions.
7. RBI also determines, in conjunction with the Central Government, the monetary and credit policies keeping in mind the need of the house.
8. The Main features of RBI are as follows:
 - (a) RBI's motive is service motive and not to earn Profit.
 - (b) RBI is owned by Government and the same is managed by persons appointed by the Central Government.
 - (c) RBI controls entire banking industry thereby controls all the activities of all kinds of banks.
 - (d) As currency issue decision is under the control of RBI, it controls the value of the currency.
 - (e) RBI undertakes financial activities in consultation with Central Government.
 - (f) Economic policies of the Government have been made successful through RBI by the Government.
9. Need of RBI in India arises because of the following reasons:
 - (a) Regulation of Monetary, Fiscal and Trade Activities.

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- (b) Controlling all kinds of banks against indiscriminate credit expansion.
- (c) Maintain value of currency both within India and outside India.
- (d) Protection of depositors' interest, thereby creating confidence in the banking industry.
- (e) Help the government by way of providing finance in both Indian Currency and Foreign currency to meet its various requirements.

10. Important functions of RBI are as follows:

- (a) Issue of Currency
 - A. RBI is solely responsible to issue Indian Currency. Issue of currency depends on maintaining certain number of reserves in the form of Gold and Foreign Exchange.
 - B. Every currency issued by RBI is its liability, as it is nothing but Promissory Note.
 - C. With reference to Note Issue, RBI adopts the following Principle:
 - (i) Currency Principle: RBI is supposed to issue the currency to the value of Gold and Foreign Currency.
 - (ii) Banking Principle: In day-to-day banking business, all the depositor's money should be lent, except keeping few monies as cash.
- (b) Acts as Banker to Government
 - A. RBI is the banker to both Central Government (CG) and State Government (SG).
 - B. RBI maintains accounts of CG and SG.
 - C. Receipts of income and payments towards expenditure of CG and SG will be monitored by RBI.
 - D. Sometimes RBI gives Overdraft Loan to CG as well as SG.
 - E. When CG and SG want to go for long term borrowings from Market, they must approach the Market borrowing only through RBI.
 - F. RBI provides various Financial Assistance to CG and SG.

(c) Acts as Banker to Banker

- A. RBI is responsible for the development of Banking sector in India.
- B. Banking principles of the Banking industry must be decided by RBI.
- C. Banking license must be given only by RBI.
- D. Only Genuine Banks are allowed to carry on the Banking Business in India by RBI.
- E. RBI is the custodian of Commercial Banks and all types of Banks.
- F. Banks must follow the guidelines and instructions of RBI to carry out its banking business in India.
- G. Money market is strengthened in India only with the healthy relationship between RBI and Commercial Banks.

(d) Lender of Last Resort

- A. RBI is said to be lender of last resort, when Banks approach it during any financial crisis.
- B. When banks exhausted all its various options to raise funds, they have no other option but to rely on the RBI.
- C. In case of any types of panic situation created against the banks due to some financial crisis, RBI must and will step in to save the Banks by discounting their bills.
- D. This act of RBI is called as “Lender of Last Resort”.

(e) Controller of Credit

- A. When Banks increase the lending activity, money supply in the economy will increase. It will lead to an inflationary trend. When prices go up, automatically it has got direct impact on curtailment of savings of public.
- B. Because of increase in price of domestic product, the demand from foreign buyers will also be getting reduced. This is because when foreign products become cheaper than the domestic

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products, import will increase. Because of this import decision, Indian industries will suffer.

- C. Hence, RBI plays a very vital role in controlling of credit of all kinds of banks.
- D. RBI helps to control inflation through the operations of Banking sector, thereby helps the country from coming out of inflation.

(f) Arranges Clearing House Facility:

- A. Cheque/Demand Draft Collection facilities have been carried out as per the instruction of RBI.
- B. This Function of RBI ensures smooth flow of funds from one Customer account to another customer account as well as from one bank to another Bank.
- C. Clearing funds have been supervised and guaranteed by RBI to all Banks.
- D. Clearing House rules and regulations have been defined and designed by RBI.

(g) Custodian of Foreign Exchange:

- A. It is the responsibility of RBI to maintain foreign currency Holding in India.
- B. Foreign Currency transactions must be carried out as per Foreign Exchange Management Act.
- C. It is the responsibility of RBI to maintain 'Favourable' Foreign Currency Position in India.
- D. Rupee fluctuations against foreign currency will be closely monitored by RBI, so that in Global economy, our Indian Currency will have very good value.

11. Periodical inspections of banks under section 35 of the Banking Regulation Act, 1949 are undertaken as a follow-up of the bank licensing regulation and objectives as laid down in section 22 of the Banking Regulation Act, 1949. The substantive objective of the statutory inspections has been to verify whether the conditions subject to which the bank has been issued licence to undertake banking business in

terms of sub-section (3) of section 22 [including sub-section (3A) for foreign banks] continue to be fulfilled by it. The conditions include:

- (a) the bank “is or will be in a position to pay its present or future depositors in full as their claims accrue” (i.e., it is solvent and has adequate liquidity).
- (b) the bank “has adequate capital structure and earning prospects”.
- (c) “The affairs of the (banking) company are not being, or are not likely to be, conducted in a manner detrimental to the interests of its present or future depositors”, and
- (d) “The general character of the management of the bank is not prejudicial to the public interest or the interest of its depositors” (i.e., it has sound operational systems and adequate controls operated by a prudent management).

12. Section 22(4) of the Banking Regulation Act, 1949 authorises the RBI to cancel the banking licence “if at any time, any of the conditions referred to in sub-section (3) and sub-section (3A) is not fulfilled”.
13. Based on the recommendations of a High-Level Steering Committee (HLSC) for Review of Supervisory Processes of Commercial Banks, the Reserve Bank of India had in September 2012, introduced a Supervisory Program for Assessment of Risk and Capital (SPARC) for commercial banks. This Risk Based Supervision (RBS) approach, helps the regulator in focusing on evaluating both present and future risks, identifying incipient issues and facilitating prompt intervention/ early corrective action - as against the earlier compliance-based and transaction testing approach (CAMELS) which was more in the nature of a ‘point in time’ assessment. The RBS approach also benefits the regulator by optimizing its use of supervisory resources and assisting the regulated entities in improving their risk management systems, oversight and controls.
14. RBI is empowered under section 21 of the Banking Regulation Act, 1949, to control advances by banks, in general, or by any bank. Among the measures that the RBI can adopt for this purpose are to prescribe purposes and extent of advances, margin requirements, maximum exposure to a single borrower, rate of interest and other terms and conditions, etc. Besides these measures (which are usually called ‘selective credit control’ measures), RBI also controls the total volume of

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bank credit by varying bank rate through open market operations or by varying cash reserve and similar requirements.

15. Bank rate refers to the rate of interest at which the RBI re-discounts the first-class bills of exchange or other eligible instruments from banks. Variations in Bank rate affect the interest rates charged by banks – generally, interest rates of banks move up or down in tandem with movements in bank rate.
16. Under Base Rate system which came into effect from July 1, 2010, all categories of domestic rupee loans of banks are priced only with reference to the Base Rate, subject to certain conditions. For monetary transmission to occur, lending rates must be sensitive to the policy rate. At present, banks follow different methodologies for computing their Base Rate like, average cost of funds method, marginal cost of funds, blended cost of funds (liabilities), etc.
17. Open market operations involve sale or purchase of government securities in the open market. When RBI buys government securities from banks in the open market, the funds in the hands of selling banks increase, enabling them to expand credit, and vice versa.
18. Banks are required to maintain at least a prescribed minimum percentage of their demand and time liabilities in India in the form of cash and/or current account balances with the RBI (called 'cash reserve ratio'). Additionally, they are required to maintain a further percentage in the form of cash and/or other liquid assets (called 'statutory liquidity ratio'). Varying the cash reserve ratio and/or statutory liquidity ratio enables the RBI to increase or decrease (as the case may be) the funds available to banks for lending and other similar purposes.
19. A major development that has implications for banks throughout the world is the "International Convergence of Capital Measurement and Capital Standards", generally, known as the Basel Accord. While the implementation of Basel 2 is expected to lead to improved risk management systems in banks, promote a more robust supervisory framework and strengthen market discipline, with the cumulative effect being greater financial stability, Basel 3 ensures better quality of capital and robust liquidity risk management. In view of its impending implementation, RBI is in a continuous dialogue with the banks regarding their preparedness to introduce the necessary up-gradation in their

internal systems, data collection machinery, quality of MIS, training facilities and availability of improved skill sets.

20. The smooth functioning of the payment and settlement systems is a prerequisite for stability of the financial system. To have focused attention on payment and settlement systems, a Board for Regulation and Supervision of Payment Systems (BPSS) was set up in March 2005.
21. The launch of the Real Time Gross Settlement System (RTGS) and NEFT (National Electronic Funds Transfer) has led to a reduction of settlement risk in large-value payments in the country. Similarly, IMPS (Interbank Mobile Payment Service/Immediate Payment Service) is a mobile based payment mechanism introduced by the National Payments Corporation of India to allow customers to transfer money instantly, facilitating instant remittance across multiple platforms. The setting up of NSDL and CDSL for the capital market settlements and CCIL for G-sec, forex and money market settlements have improved efficiency in market transactions and settlement processes. A series of legal reforms to enhance the stability of the payment systems have been carried out. With the introduction of the Payments and Settlement Act in 2008, the Reserve Bank has the legislative authority to regulate and supervise payment and settlement systems in the country.
22. In India, deposit insurance is provided by the Deposit Insurance and Credit Guarantee Corporation (DICGC), a wholly owned subsidiary of the Reserve Bank of India. Deposit insurance in India is mandatory for all banks (commercial/co-operative/RRBs/LABs). It covers all kinds of deposits except those of foreign governments, Central/State Governments, inter-bank, deposits received abroad and those specifically exempted by DICGC with prior approval of the Reserve Bank. The premium charged for deposit insurance is on a flat rate basis, which is currently 10 paise per `100 of assessable deposits with a statutory ceiling on premium at 15 paise. The premia to be paid by the insured banks are computed based on their assessable deposits. Insured banks pay advance insurance premia to the Corporation semi-annually within two months from the beginning of each financial half year, based on their deposits as at the end of previous half year. The amount of coverage is presently limited to Rs. 1 lakh per depositor and extends to deposits held in the same right and in the same capacity.
23. Banks and financial institutions (FIs) have also been advised by RBI to follow certain customer identification procedure for opening of accounts

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and monitor transactions of suspicious nature for the purpose of reporting the same to appropriate authority. These 'Know Your Customer' (KYC) guidelines have been revisited in the context of the recommendations made by the Financial Action Task Force (FATF) on Anti Money Laundering (AML) standards and on Combating Financing of Terrorism (CFT). Detailed guidelines based on the recommendations of FATF and the paper issued on Customer Due Diligence (CDD) for banks by the Basel Committee on Banking Supervision (BCBS), with suggestions wherever considered necessary, have been issued. Banks/FIs have been advised by RBI to ensure that a proper policy framework on 'Know Your Customer' and Anti-Money Laundering measures is formulated and put in place with the approval of their Boards. The objective of KYC/AML/CFT guidelines is to prevent banks/FIs from being used, intentionally or unintentionally, by criminal elements for money laundering or terrorist financing activities. KYC procedures also enable banks/FIs to know/understand their customers and their financial dealings better and manage their risks prudently. Foreign Account Tax Compliance Act (FATCA) is a US law, which was enacted in March 2010 by US Government which was aimed at preventing tax evasion through offshore assets by US citizens and US residents. Foreign Financial Institutions (FFIs) such as the Bank that enter into a FATCA FFI agreement with the US government are required to conduct certain due diligence to identify its US clients (individual and entity) and report on their accounts to the US Internal Revenue Service (IRS).

24. India has signed the Inter-Governmental Agreement (IGA) with USA for improving international tax compliance and implementing the Foreign Account Tax Compliance Act (FATCA). India has also signed a multilateral agreement on June 3, 2015, to automatically exchange information based on Article 6 of the Convention on Mutual Administrative Assistance in Tax Matters under the Common Reporting Standard (CRS), formally referred to as the Standard for Automatic Exchange of Financial Account Information (AEOI).
25. Apart from directions relating to operational matters, RBI also issues, from time to time, guidelines on accounting matters to be followed by banks. These guidelines have a profound effect on annual accounts of banks. The text of the notifications/circulars/guidelines, etc., issued by the RBI are normally also available on its website www.rbi.org.in.

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Note:

1. All the Members/ Readers who are referring this manual, for updating Please go to RBI website – Type Index to Bank circulars.
2. The members conducting bank audit are expected to update their knowledge by frequently visiting RBI website.
(<https://www.rbi.org.in/Scripts/NotificationUser.aspx>) .

Chapter 4

Legal Framework of Banks

Enactments Governing Functions of Banks

There is an elaborate legal framework governing the functioning of banks in India. The principal enactments which govern the functioning of various types of banks are:

- Banking Regulation Act, 1949.
- Banking Companies (Nationalization of Undertakings) Act, 1970.
- Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980.
- Negotiable Instruments Act, 1881.
- State Bank of India Act, 1955.
- Regional Rural Banks Act, 1976.
- Companies Act, 2013.
- Co-operative Societies Act, 1912 (or the relevant State Cooperative Act).
- Information Technology Act, 2000.
- Prevention of Money Laundering Act, 2002.
- Credit Information Companies (Regulation) Act, 2005.
- Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.
- Recovery of debts due to Banks and Financial Institutions Act, 1993.
- Transfer of Property Act, 1882.
- Indian Stamp Act, 1899.
- Power of Attorney Act, 1882.
- The Insolvency and Bankruptcy Code, 2016.
- Foreign Exchange Management Act, 1999.
- Uniform Customs and Practice for Documentary Credits (UCP 600).

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- Payment and Settlement Systems Act, 2007.
- Insurance Regulatory and Development Authority Act 1999.
- Deposit Insurance and Credit Guarantee Corporation Act 1961.
- Securities and Exchange Board of India Act, 1992.
- Fiscal Responsibility and Budget Management Act 2003.
- Government Securities Act 2006.
- Banking Ombudsman Scheme.

Besides, the above enactments, the provisions of the Reserve Bank of India Act, 1934, also affect the functioning of banks. The Act gives wide powers to the RBI to give directions to banks; such directions also have considerable effect on the functioning of banks.

Salient Provisions of Banking Regulation Act, 1949

1. Out of the above, the Banking Regulation Act, 1949 is the most important as it affects the functioning of all institutions carrying on banking business.
2. Other enactments relate only to certain specific type(s) of banks.
3. Some of the important provisions of the Act are briefly described below since familiarity with them is essential for the performance of the duties of an auditor.
4. It needs to be emphasized that the ensuing discussion is not an exhaustive discussion on all the relevant provisions of the Act.

Definition of Banking Companies

A banking company means "any company which transacts the business of banking in India" [section 5(c) of the Banking Regulation Act]. The term 'company' for this purpose covers companies registered in India as well as foreign companies, i.e., companies incorporated outside India and having a place of business within India [section 5(d)].

Forms of Business of Banking Companies

1. 'Banking' is defined as "the accepting, for the purpose of lending or

investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise" [section 5(b)]. It has been clarified that any company which is engaged in the manufacture of goods or carries on any trade, and which accepts deposits of money from the public merely for the purpose of financing its business as such manufacturer or trader, shall not be deemed to transact the business of banking [*Explanation* to section 5(c)].

2. Section 6 of the Act permits a banking company to engage in certain forms of business in addition to the business of banking. Besides the forms of business specifically listed in clauses (a) of sub-section (1) of section 6, a banking company may do "all such other things as are incidental or conducive to the promotion or advancement of the business of the company" [clause (n) of sub-section (1) of section 6]. Under clause (o), a banking company may engage in any other form of business (besides those covered by other clauses) which the Central Government may, by Notification in the Official Gazette, specify as a form of business in which it is lawful for a banking company to engage.
3. Under sub-section (2) of section 6, a banking company is prohibited from entering any form of business other than those covered by subsection (1) of the said section. Section 8 specifically prohibits a banking company from buying, selling or bartering goods except in connection with the realization of a security held by it. It also prohibits a banking company from engaging in any trade or buying, selling or bartering of goods for others except in connection with collecting or negotiating bills of exchange or in connection with undertaking the administration of estates as executor, trustee or otherwise. However, the above prohibitions are not applicable to any business specified by the Central Government in pursuance of clause (o) of sub-section (1) of section 6.

Licensing of Banking Companies

Section 22 of the Act prohibits a company from carrying on banking business in India unless it holds a license issued by the RBI. The license may be a conditional license. The license may be cancelled if the company ceases to carry on banking business in India or fails to comply with the conditions of the license or fails to fulfil any other condition laid down in the section.

Inspection by the RBI

Wide powers have been given to the RBI under section 35 for inspection of

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any banking company and its books and accounts. The Central Government can also direct the RBI to cause such an inspection.

Power of the RBI to give Directions

- The RBI is empowered to issue such directions to banking companies generally or to any banking company in particular as it deems fit in public interest, or in the interest of banking policy, or to prevent the affairs of any banking company from being conducted in a manner detrimental to the interests of the depositors or in a manner prejudicial to the interests of the banking company, or to secure the proper management of any banking company generally (Section 35A).
- The RBI is also empowered to caution or prohibit banking companies generally or any banking company against entering into any particular transaction or class of transactions and generally give advice to any banking company [Clause (a) of sub-section (1) of Section 36].

Provisions relating to Accounts and Audit

- Section 29 of the Act lays down requirements as to profit and loss account and balance sheet.
- Section 30 deals with audit of Profit and loss account and Balance sheet prepared in accordance with section 29.
- Section 31 deals with publication of Profit and loss account and Balance sheet and their submission to RBI.
- Section 32 deals with submission of Profit and loss account and Balance sheet to Registrar of Companies.
- Section 33 deals with display of audited Balance sheet and Profit and loss account by companies Incorporated outside India and carrying on banking business in India.

It may be noted that some of the above provisions are not applicable to nationalized banks, State Bank of India, subsidiaries of State Bank of India, regional rural banks, and co-operative banks.

Other Important Provisions of the Banking Regulation Act, 1949

Besides the above provisions, a few other provisions of the Act are relevant to the work of the auditor. Some of the important, provisions are:

Section 9	Disposal of non-banking assets (Banks are prohibited from holding any immovable property, other than assets for its own use and should dispose of the assets held in satisfaction of claim within 7 years or ' such extended period as RBI allows).
Section 13	Restriction on commission, brokerage, discount and remuneration etc., on the issue of shares up to 2.5 % of the paid-up value of the shares.
Section 18	Cash Reserve to be maintained.
Section 19	Restriction on the nature of business of subsidiary Companies.
Section 20	Restriction on Loans and advances Restriction on power to remit debts owed by directors and related enterprise.
Section 21	Power of RBI to control advances of Banking companies.
Section 24	Maintenance of a percentage of (liquid) assets.
Section 25	Quarterly return of Assets in India.
Section 26	Return of unclaimed deposits (including non-operative accounts being older than 10 years or more).

Returns to be Submitted to the RBI

1. The Banking Regulation Act, 1949 requires banking companies, nationalized banks, State Bank of India, its subsidiaries, and regional rural banks to furnish the following returns to the RBI:
 - (a) Monthly return of assets maintained in India in accordance with section 24 and demand and time liabilities in India at the close of business on each alternate Friday during the month. [Section 24]
 - (b) Quarterly return of assets and liabilities in India at the close of business on the last Friday of every quarter. [Section 25]

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- (c) Annual return of unclaimed accounts which have not been operated for 10 years. [Section 26]
 - (d) Monthly return of assets and liabilities in India at the close of business on the last Friday of every month. [Section 27]
2. The above types of banks have also to furnish such other statements or information as may be required by the RBI under section 27 of the Act. In exercise of its powers under the aforesaid section, the RBI requires many returns to be furnished to it. Some of the important returns required to be furnished to the RBI are as enumerated below, with their periodicity indicated in parentheses:
- (a) Report on Non-Performing Advances (annual).
 - (b) Statement showing the position of reconciliation of investment account (annual).
 - (c) Statement on compromises and settlements involving write-off (half yearly).
 - (d) Statement on bad debts written off (annual).
 - (e) Details of Doubtful or Loss Assets and Suit Filed accounts with outstanding aggregating `1crore and above(half-yearly).
 - (f) Details of remittance of profits / surplus retained in India(annual).
 - (g) Particulars of provisions held on problem credits of overseas branches (half-yearly).
 - (h) Inter-branch reconciliation (quarterly).
 - (i) Reconciliation of outstanding inter-branch accounts (annual).
 - (j) Reconciliation of clearing differences (annual).
 - (k) Position of balancing of books (quarterly).
 - (l) Returns relating to frauds, robbery, etc. including fraud involving` one crore and above (quarterly).
 - (m) Return of Capital Adequacy (quarterly).
 - (n) Return on Asset Quality (quarterly).

- (o) Asset-liability management (monthly).
- (p) Return in respect of Statutory Liquidity Ratio (monthly).

Online Reporting to RBI Through 'ORFS' and 'XBRL'

1. As a regulatory and supervisory function bestowed on RBI, it collects returns from commercial banks, financial institutions, etc. Many of these returns are the statutory requirement under Reserve Bank of India Act ,1934, Banking Regulation Act,1949, FEMA ,1990.
2. The conventional method of return submission requires sending of hard copy through postal services, fax and PDF file through e-mail. All these modes of filing returns have their own limitations. Hence, the need was felt for developing the single electronic return submission window 'ORFS' (Online Filing System).
3. As a part of online filing of returns, the Reserve Bank of India felt the need for the adoption of best internet technology solution. Thus, RBI has adopted 'XBRL' (extensible Business Reporting Language) which attends the standardization of business reporting especially Financial Reporting. While 'ORFS' brings no standardization across all the returns, 'XBRL' can implement global standards across all returns. Today, these two online systems, i.e., 'ORFS' and 'XBRL' coexists and now the ORFS is in the process of being phased out. Most of the returns are mandatorily XBRL based with reporting now increasingly centralised through RBI DAKSH.

Chapter 5

Know Your Customer (KYC) Policy

Introduction

1. RBI on 25.2.2016 has issued Master Direction – Know Your Customer Directions, 2016.
2. Later on, various Circulars and directions have been issued by RBI with updation. Before going to understand the KYC policy, every Concurrent Auditor must go through the Master circulars RBI/DBR/2015-16/18 Master Direction No. DBR.AML.BC.No.81/14.01.2001/2015-16 dt February 25, 2016 updated on June 12, 2025 along with FAQs on Master Direction on KYC issued by RBI on June 9, 2025.
3. The provisions of Prevention of Money-Laundering Act (PMLA), 2002 and the Prevention of Money Laundering (Maintenance of Records) Rules, 2005 have been covered and mentioned in “Master Direction-Know Your Customer (KYC) Directions 2016 as amended from time to time.
4. Customer Due Diligence (CDD) process has been updated as per updation in PML Rules by government. Master Direction is updated considering changes in Unlawful Activities (Prevention) Act (UAPA) 1967 & instructions in accordance to Financial Action Task Force (FATF) recommendations. The definition of Politically Exposed Person (PEP) is introduced and accordingly Customer Due Diligence Process has been updated (CDD).
5. Whenever Regulated Entities (RE) (as defined in para below) open the Account or carryout any transaction with the Customers, they must identify the Customers. This will help the RE to monitor all kinds of financial and non-financial transactions.
6. As per the Powers conferred by Section 35A of Banking Regulation Act, 1949, read with Section 56 of the Act and Rule 9(14) of Prevention of Money Laundering (Maintenance of Records) Rules 2005, RBI has introduced the concept of KYC. At the time of introducing the concept of KYC, RBI considered the public interest and REs.

Know Your Customer (KYC) Policy

7. KYC is highly important considering the money laundering offences and controlling the funding for terrorist activities.
8. **Regulated Entities** mean:
 - (a) All Scheduled Commercial Banks (SCBs).
 - (b) Regional Rural Banks (RRBs).
 - (c) Local Area Banks.
 - (d) All Primary (Urban) Cooperative Banks.
 - (e) Any other Entity Licensed u/s 22 of the Banking Regulations Act, 1949.
 - (f) State & Central Co-operative Bank (StCBs & CCBs).
9. Few of the Regulated Entities Licensed u/s 22 of the Banking Regulations Act, 1949:
 - (a) Non-Banking Finance Companies (NBFC).
 - (b) Miscellaneous NBFC (MNBC).
 - (c) All types of Authorised Persons which include the Agents of Money Transfer Service Scheme, who are regulated by the Regulator (RBI).
10. Who is a customer of Banks (RE):

For the purpose of KYC policy, a 'Customer' is defined as:

- a person or entity that maintains an account and/or has a business relationship with the bank.
- one on whose behalf the account is maintained (i.e. the beneficial owner).
- beneficiaries of transactions conducted by professional intermediaries, such as Stockbrokers, Chartered Accountants, Solicitors etc. as permitted under the law, and
- any person or entity connected with a financial transaction which can pose significant reputational or other risks to the bank, say a wire transfer or issue of a High value DD as a Single Transaction.

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11. Few of the Important Regulators in India are as follows:

Regulatory Body	Sector
1. Reserve Bank of India (RBI)	Banking and Finance
2. Securities & Exchange Board of India (SEBI)	Stock and Capital Market
3. Insurance Regulatory & Development Authority of India (IRDA)	Insurance
4. Pension Fund Regulatory & Development Authority (PFRDA)	Pension
5. National Bank for Agriculture & Rural Development (NABARD)	Financing and Rural Development
6. Insolvency and Bankruptcy Board of India (IBBI)	Insolvency Proceedings

Objective of KYC

1. The main objective of KYC Guidelines is that the Banks, Intermediaries and Financial Institutions should not be used by Criminal elements for Money Laundering activities, terror financing, proliferation financing or other related risks.
2. Mitigation & Management of Risks.
3. By following KYC guidelines, suspicious nature of Money transactions can be easily identified.

Key Elements of KYC

There are 4 Key Elements of KYC:

1. Customer Acceptance Policy.
2. Risk Management.
3. Customer Identification Process.
4. Monitoring of Transactions.

1. Customer Acceptance Policy

- (a) It is the Basic Criteria designed by RE for a customer to enter or terminate from the RE (banks) to maintain customer relationship.
- (b) This policy and documents should be designed in such a manner that Anonymous or fictitious or Benami/mule customers or accounts thereof are restricted to have any relationship with the Banks.
- (c) Banks must carry proper due diligence at the time of opening the accounts for their customers. In case, the Customers have not cooperated or not submitted the required documents as per KYC policy, the Banks are not allowed to open the Bank account for those customers. KYC policy is clear that the Bank accounts will be allowed to be open only when proper Due Diligence of the customers are carried out.
- (d) Banks should not deny opening the Bank account, just because the customers are financially or socially disadvantaged.

2. Risk Management

- (a) RE to design & develop processes to verify Digital Sign in case the customer submits e-documents.
- (b) Banks REs) should have a risk-based approach to classify the customers.
- (c) Bank customers have been classified as Low, Medium and High-risk customers. This is based on the Assessment and risk perception of Banks.
- (d) Customer risk status will not be /should not be informed to the customers by the Banks.
- (e) Customer risk is being arrived at on Money Laundering risk associated with a particular customer from Bank's KYC perspective.
- (f) The Customer risk is being considered at the time of opening the account or during the operations of the account.
- (g) KYC updation for the customers must be obtained based on the Category of risk involved which are as follows:

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Risk Category of Customers	Once in ____ Years	Updation period Depends on Banks' KYC Policy **
High	2	Yes
Medium	8	Yes
Low	10	Yes

**This updation period varies according to Bank as per the instructions of RBI.

(h) The parameters for risk fixation are based on the following:

- Customer identity.
- Social/Financial Status.
- Nature of Business Activity.
- Nature of Business and Location.
- Type of Product & Services offered.
- FATF (Financial Action Task Force) Public Statements.
- Regulated Authorities Search and Raids.
- Regulated Authorities Blacklisted Customer List.
- Regulated Authorities Willful Defaulter List.
- NPA Customers.
- Indian Bank Association's reports and guidance notes on KYC/AML.
- RBI's guidance Notes circulated to all Cooperative Banks.
- Any other Parameter as decided by Banks (RE).

3. Customer Identification Process (CIP)

- (a) This procedure has to be carried out before opening the account or during the account operation by the customer.
- (b) This CIP creates financial relationship between Bankers and customers.

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- (c) This CIP applies to both New as well as Existing customers. This process includes identification of –
 - (i) Account Holder
 - (ii) Non-Account Holder
 - (iii) Customer to whom third party product sold
 - (iv) Walk in customer
- (d) In case of CIP Procedure, REs shall ensure that introduction is not to be sought while opening accounts.
- (e) In case the Bank has got doubts about the Customer or his/her/its transactions, a fresh CIP has to be carried out by the Bank (RE).
- (f) Sometimes there are walk-in customers who do not have any account with the Bankers. i.e. they are visiting the branch to remit money into the account (Rs.50000 or more) either to remit the same in the Bank's account holder account or to take Demand Draft or NEFT or RTGS. In this situation also the Bankers (RE) must carry out CIP carefully before entering into the financial transaction with those walk-in customers. This CIP is being used to verify the Financial Transactions carried out by the Third-Party customers.
- (g) Customers at Remote Places can give Video based Customer Identification Process (V-CIP) which is also another method of KYC CIP verification.

4. Monitoring of Transactions (MOT)

- (a) MOT has to be carried out by Banks in all the financial transactions which exceed "threshold limits" prescribed for specific category of accounts.
- (b) RBI has instructed Banks to set Key indicators for risk sensitive accounts. Key indicators have been fixed based on the High Turnover involved in the accounts or due to the complexity of accounts or unusual transactions carried out in the accounts.
- (c) Banks at the time MOT must take the full background of the Customer (New as well as Existing) which includes Customer's country of origin, Source of Funds, Type and Nature of transactions carried out and other risk factors of the account as per Bank's policy.

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- (d) Periodical review and Due Diligence of the Customer account must be carried out by Banks at least not less than once in 6 months. This exercise must be carried out from the Risk categorization of customers.
- (e) In case of Non-cooperation by the customers with reference to KYC, the Bank account can be closed by the Banks after giving due notice to the Customer.
- (f) The process of Partial Freezing of Customer (PFC) Account due to Non submission of KYC documents:
 - The Banks must give Notice to Customers of 3 Months initially before exercising the option of Partial Freezing.
 - A further time of 3 months has also to be given to the customer by mentioning in the First Notice and its conditions.
 - Due to non-cooperation/non submission of KYC documents, the customer account is put on hold saying as “Partial Freezing”.
 - In the “Partial Freezing” account, the Bank allows only Credit (Receipt) into the account and No Debit (withdrawal) is allowed.
 - The Bankers must treat these types of PFC accounts as ‘Inoperative account’. If the accounts are still KYC non-compliant after six months of imposing initial ‘partial freezing’ banks may disallow all debits and credits from/to the accounts, rendering them inoperative. Hence, the account will become Inoperative only after imposing debit as well as credit freeze in the account and not on account of partial freezing only which is freezing debit transactions and allowing credit transactions in the account.
 - The Bankers must send the letters to the Customers (on the last known address) to close the accounts.
 - PFC accounts can be reactivated by the Bank if the customers have produced all the required KYC documents and other details as requested by the Bank.
 - The REs is expected to undertake on going Due Diligence of customers to ensure the transactions are consistent with their knowledge about the customers.

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- The REs is expected to conduct Enhanced Due Diligence for the accounts to be open on face-to-face basis i.e. through V-CIP or by digital channels.

5. Other Important Points and Highlights of KYC

- (a) In case the customer has refused to submit the required KYC documents before opening the accounts, Bankers have got full right to reject the Account Opening application submitted by the Customers and refuse to open the account.
- (b) Introduction of account is not required in case “e KYC” is being carried out.
- (c) A customer has all his KYC documentary evidence at One place (say Mumbai) and he wants to start his business at another Place (say Chennai). The customer who is at Mumbai has declared that Mumbai address is Permanent address and Chennai address as Official Address. For both Permanent address and Official address, the customer must give Proof. Bankers have got no right to reject the Opening of the account that KYC is not available at Chennai.
- (d) In case the Customer wants to transfer his account from one Branch to another Branch of the Same Bank, no Fresh KYC is required, provided he operates the accounts from the same address. In case the customer changes his Business/residential address, then he must submit KYC documentary proof with the Changed address.
- (e) Banks must specify their risk-based approach in the KYC policy, especially the periodic updation of KYC. Any additional measures, such as the requirement of obtaining recent photographs, requirement of physical presence of the customer, requirement of periodic updation of KYC only in the branch of the RE where account is maintained, a more frequent periodicity of KYC are also to be specified in the Board approved internal KYC policy.
- (f) In case of no change in KYC information, at the time of periodic updation of KYC, a self-declaration from Individuals, and resolution etc. in case of other than individuals is sufficient.
- (g) In case the Branch of the Bank has obtained KYC for One account, and the Customer wants to open another account, there is no need to submit another set of KYC:

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- PAN must be quoted for all cash deposit transactions if it is Rs 50000 or more.
- KYC Norms are applicable for both Debit Card and Credit Card.
- For Any foreign remittance from India to Abroad, KYC exercise must be done by the Banks (RE).
- RBI in its release on 5.1.2023 has advised banks to provide the facility of self-declaration (for re-KYC) to individual customers through various non-face-to face channels like Registered email ID, Registered Mobile Number, ATMs, online banking, internet.
- Know Your Business:
 - GST Registration for all people except New Proprietors.
 - Udyam Registration Certificate for all Sole Proprietors including NEW entrepreneurs.

6. Concurrent Auditor Verification and Certification on KYC

Note:

1. KYC policy of the bank is to be verified at the beginning of the audit of the particular bank. Highlights of Bank specific policy to be noted and verified such as frequency of periodic verification, obtaining of various documents for monitoring of accounts etc. The frequency and manner of carrying out monitoring exercise as per 'Money Laundering (ML) and Terrorist Financing (TF) Risk Assessment' should also be understood and verified while carrying out concurrent audit.
2. Branch Manager /Official must ask for the Original and photostat copies to be produced and certify on the photostat copies that he /she has verified the original and affixed his full signature with Bank seal on all the photostat copies.
3. Abnormal transactions are to be checked, especially for newly opened accounts with a specific reference to 'Money mules', Multilevel marketing etc.
4. Carefully ascertain the following points: A. Cross verification of actual dispatch of 'welcome packs' to new customers or whether handed over to customer in the branch itself. Outward register to be

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checked for dispatch. B. in case of Central processing of KYC, the process of sending documents to be ascertained. Policy of bank to mitigate Data loss or documents loss in loss to be ascertained. C. Process of the bank for record preservation in case of KYC updation of Inoperative accounts to be checked.

5. Branch Manager /Official must certify that the Bank customer has signed the photostat copies of all the KYC documents as “True Copy” in his presence, i.e., self-attestation by the customer.
6. It is the duty of the Concurrent Auditor to verify all those KYC documents and must report the irregularities without fail. If the Concurrent Auditor fails to report the irregularities in KYC documents and if anything goes wrong in future, then Concurrent Auditor will be held responsible by Bank’s Head Office, RBI, ICAI (under disciplinary proceedings), Regulatory Authorities and Court.

7. Details to be given in all applications – Individual/ Partner/ Director/ Trustee/ Authorised Person

1. Name
2. Father’s Name/Husband’s Name
3. Complete Address with PIN code
4. PAN
5. Aadhar Number
6. Mobile Number
7. Valid email-id
8. Source of Income
9. Basic KYC Documents required to be obtained by Banks, and it is the duty of the Concurrent Auditor to verify the same.

(The following is only a Checklist, and the Concurrent Auditor can ask for additional details to satisfy about the Genuineness of the Customer. Moreover the Concurrent Auditor should go through the updated master direction dt June 12, 2025, by RBI for the requirement of KYC documentation)

A. Individual

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1. *PAN Card.*
2. *Aadhar Card.*
3. *Passport.*
4. *Driving License.*
5. *If the Customer has come from other areas/State, then the Signature must be attested by his existing Bankers (So Bankers have to ask the customer to produce his /her other Bank details).*
6. *Residential and Office Address Proof: Customer must produce, Electricity Bill, Property Tax Receipt, Telephone Bills, Rent Agreement in case the House is a rented one.*
7. *Address Proof duly certified by Supreme Court/High Court/District Court Judges, MP/MLA in case no address proof is available.*
8. *One of the Proof should have Photo identity.*
9. *GST Registration certificate.*
10. *Udyam Registration Certificate.*
11. *Import and Export Code – if the individual is going to do export and import business.*

B. Partnership Firm

1. *Partnership Deed.*
2. *Firm Registration Certificate – see the validity.*
3. *PAN Card for the Firm.*
4. *Partner's KYC – as stated in Individual KYC category above.*
5. *Address Proof of the Firm – Rent agreement/ Ownership evidence/ Utility Bills.*
6. *Power of Attorney Appointment Letter – Granted to any person other than the Partners.*
7. *KYC of Power of Attorney Holder – as stated in Individual KYC category above.*

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8. *GST Registration Certificate.*
9. *Udyam Registration Certificate.*
10. *Import and Export Code – if the Partnership Firm is going to do export and import business.*

C. Hindu Undivided Family (HUF)

1. *PAN card for HUF.*
2. *PAN card for Kartha of the Family.*
3. *Affidavit declaring the list of Co-parceners of the HUF.*
4. *KYC of all the Co-parceners – as stated in Individual KYC category above.*
5. *Photo of Kartha duly attested by Co-parceners of HUF.*
6. *HUF Deed.*
7. *GST Registration Certificate.*
8. *Udyam Registration Certificate.*
9. *Import and Export Code – if the HUF is going to do export and import business.*

D. Limited Companies (Private or Public)

1. *Certificate of Incorporation (With CIN) – ROC Certificate.*
2. *Certificate of Commencement Letter (with CIN) – ROC certificate in case of Public Limited company.*
3. *Memorandum and Articles of Association.*
4. *PAN of the Company.*
5. *Address proof of company –*
 - a. *Rent Agreement in case the company is functioning in rented premises, along with House tax receipt/ Utility Bills*
 - b. *If the business is carried out in the own premises of the company, provide Title deed copy, House tax receipt/ Utility Bills*
6. *KYC of All directors – as stated in Individual KYC category above.*

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7. *Director Identification Number – Each director.*
8. *ROC Forms for Directors appointment.*
9. *Board Resolution to open the accounts.*
10. *Board Resolution regarding Account operation Authorisation given to Board of Directors/ Financial Officers/ Others.*
12. *Import and Export Code – if the Company is going to do export and import business.*
13. *GST Registration certificate.*
14. *Udyam Registration certificate.*
15. *Other licenses available, if any.*

E. Limited Liability Partnership

1. *Certificate of Incorporation with LLPIN and DPIN of the Designated Partners.*
2. *LLP Agreement.*
3. *Permanent Account Number of LLP.*
4. *Designated Partners – KYC as mentioned in Individual category above.*
5. *Address Proof of LLP:*
 - (a) *Rent Agreement in case the LLP is functioning in rented premises, along with House tax receipt/ Utility Bills*
 - (b) *If the business is carried out in the own premises of the LLP, provide Title deed copy, House tax receipt/ Utility Bills*
6. *Power of Attorney of Designated Partners to operate the Account.*
7. *Resolution to operate the Bank account by the Designated Partners.*
8. *Import and Export Code – if the LLP is going to do export and import business.*
9. *GST Registration certificate.*
10. *Udyam Registration certificate.*

11. *Other licenses available, if any.*

F. Association of Person

1. *AOP agreement, if any.*
2. *PAN of AOP.*
3. *KYC of AOP members – KYC as mentioned in Individual category.*
4. *Power of attorney letter authorizing a person to act on behalf of AOP, duly signed by all members of AOP.*
5. *Resolution copy to operate AOP bank account at AOP Members meeting.*
6. *Import and Export Code – if the AOP is going to do export and import business.*
7. *GST Registration certificate.*
8. *Udyam Registration certificate.*
9. *Source of creation of AOP.*
10. *Other licenses available, if any.*

G. Body of Individual (BOI)

1. *PAN of Body of Individuals.*
2. *Individual BOI members - KYC as mentioned in Individual category.*
3. *Status of Body of Individual – Prove with evidence.*
4. *Import and Export Code – if the Body of Individual is going to do export and import business.*
5. *GST Registration certificate.*
6. *Udyam Registration certificate.*
7. *Other licenses available, if any.*
8. *Source of creation of BOI.*

H. Society

1. *Society Registration Certificate.*

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2. *Society Bye Laws.*
3. *Society Members List.*
4. *Society Members KYC – As applicable in Individual status stated above.*
5. *PAN – Society.*
6. *Import and Export Code – if the Society is going to do export and import business.*
7. *GST Registration certificate.*
8. *Udyam Registration certificate.*
9. *Other licenses available, if any.*

I. Trust

1. *Trust Registration Certificate.*
2. *Trust Bye Laws /Deed.*
3. *Trust Members List.*
4. *Trust Members KYC – As applicable in Individual status stated above.*
5. *PAN – Trust.*
6. *Import and Export Code – if the Trust is going to do export and import business.*
7. *GST Registration certificate.*
8. *Udyam Registration certificate.*
9. *Other licenses available, if any.*

J. Non-Resident Indian

1. *KYC as applicable to Individual status stated above.*
2. *Passport copy.*
3. *Visa Copy.*
4. *Overseas Address Proof.*
5. *Bank account details (before attaining NRI Status).*

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6. *Person of Indian Origin (PIO) certificate.*
7. *Employment Appointment Letter to work abroad, if any.*
8. *Business Registration certificates, if NRI is doing the business in abroad.*
9. *If the documents have been signed out of India by NRI, signature must be attested by Embassy officials/ Notary Public (depends on the Laws of foreign country).*
10. *Obtain copies of Passport once in 3 years – to verify the NRI status.*

K. Foreigner

1. *Passport of Foreigner.*
2. *Visa certificate of Foreigner.*
3. *RBI permission to open the Bank account.*
4. *Certificate issued by Foreigner's bank about the integrity and his /her account details.*
5. *If the documents have been signed out of India by Foreigners, signature must be attested by Embassy officials/ Notary Public (depends on the Laws of foreign country).*
6. *Residential Status Card of Foreigner.*

L. Minor Account

1. *Minor – KYC -applicable to Individual status as stated above*
2. *Age Proof Evidence.*
3. *Guardian – KYC applicable to Individual Status as stated above.*
4. *Joint Photograph with Minor and Guardian.*

M. Legal Heir Account

1. *Death Certificate of the Customer.*
2. *Legal Heirship certificate of the Customer.*
3. *Legal Heirs – KYC applicable to Individual status as stated above.*
4. *Cheque Operation Letter as authorized by all the Legal Heirs.*
5. *Consent to continue the account of the deceased customer by the legal heirs – if the account is allowed to be operated.*
6. *Court Order, if any, in case any of the legal heir is a Minor.*
7. *Photos of all the Legal Heirs.*

N. Nominee Conversion Account

1. *Death certificate of the Customer.*
2. *Nominee – KYC as applicable to Individual status stated above.*
3. *Photo/s of Nominees.*

O. Government Accounts

1. *Document showing the name of the person to act on behalf of the entity.*
2. *Officially valid documents for proof of identity and address in respect of person holding a power of attorney to transact on its behalf.*
3. *Such documents as may be required by the Bank to establish the legal existence of such entity/juridical person.*

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4. *Resolution passed/ Power given by the Higher authorities to the Authorised Person to operate the Bank account.*
5. *Authorised Signatory – KYC details as applicable to individual status.*
6. *Photo of the Authorised Signatory.*

Chapter 6

Internal Control, Inspection and Internal Audit

Internal Control

The internal control mechanism of any organization refers to the procedures, protocol and documentation standards designed to ensure orderly and efficient conduct of the business, ensure adherence to Regulatory guidelines timely preparation and completion of accounting records by safeguarding the assets and interest of the organization, enable Risk-Based decision making and prevention and detection of errors and fraud by strengthening governance and accountability.

Currently banking business in India, led by digital transformation and in view of the cyber and financial frauds have emphasised on robust internal control and audit systems to improve operational efficiency, align with Basel III and RBI norms, and improve the depositor and investor confidence.

Given the increasing reliance on digital platforms within banks' support functions, it is imperative to establish robust internal controls.

These should encompass structured user education and training programs, implementation of effective digital access and operational controls, a comprehensive Disaster Recovery Plan to address system downtimes, and a well-defined whistle-blower mechanism to report anomalies and risks.

In our country, a robust system of internal control, internal check and documentation procedures is already in vogue in the banking industry. The responsibility of the concurrent auditor would be confined to the substantive and compliance test to ensure adherence to the internal control procedures by the banks. However, it is imperative that the auditor should verify and ensure the efficacy of the system running in the bank / branch. In addition to this, it is a challenge for the auditor to ensure the accuracy of granular data fed into the system master.

The data fed into the master for various parameters like rate of interest, interest rest, operational instructions, EMI, initial holiday of repayment; if any, etc. are of high significance in ensuring the internal controls of the banking system in a computerized environment.

The control functions commence initially from adherence to the KYC norms. The identity and authenticity of the customers and their credentials, including the basic data are of paradigm importance to establish controls in respect of ensuring details of the customer/ person dealing with the bank. Further, the internal control procedures extend to the following functional areas of a bank:

- Deposits
- Advances
- Support Functions
- Regulatory Compliance
- System Controls
- Housekeeping

Deposits

The internal controls in respect of accepting deposits are focused on the identification of the depositor and adherence to KYC norms. It is also important that the mode of receipt of deposit, its term and the compliance of the Anti-Money Laundering (AML) regulations should be ensured as a part of internal control procedures.

The following controls are to be ensured by the banker.

- The changes in rate of interest on deposits made from time to time should be properly kept under surveillance.
- Management of *auto renewal command* of Term Deposits should be well designed in the system and system relating to lifting of Dormancy flag by exception is properly implemented.
- The system of identification and classification of dormant accounts should be proper.
- The acceptance of cash for making high value-term deposits and its allied regulatory framework should be properly kept under control.

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- Clearance from the KYC hub for identification of the depositor should be ensured.
- The class of depositor and any incremental interest paid to senior citizens, bank staff etc. should be properly fed to the deposit master.
- The closure of the deposits before maturity, which is not properly supported by a system for calculation of interest, should be documented and authorized.
- The closure of lien marked deposit should not be allowed in the system.
- Unusual Deposit patterns to be monitored to detect suspicious activities relating to money laundering.
- Manual debit entries to Interest Paid on deposits should be scrutinized.
- Proper deduction of TDS on term deposits and other TDS related compliance like filing of ETDS returns should be verified.
- Check the modification of details relating to account holders in the computer system, like change of address, change of name, change of signature, change in contact details like mobile no. etc. are supported by proper application, supporting documentation and by way of SMS.
- Check whether updating of nominations details in the system are supported by proper authorization and documentation and auditor shall refer the amendments in the Banking Regulation Act (amended) in 2024.
- Operational instructions relating to 'High Value Deposits', their rate of interest and penalties relating to pre matured withdrawal of these deposits are properly implemented.
- Proper Value Dating of transactions relating to renewal of fixed deposits are properly implemented.
- Marking of lien in the system in case of loans/advances against fixed deposits is strictly followed. Similarly marking lien on deposits held as margins for issuance of Letters of credit and Bank Guarantees is properly ensured.

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- Provisioning for interest on overdue deposits is being done as per extant instructions issued by the Bank.
- System of collection of service charges on facilities offered to depositors like SI (Standing instructions), etc. and recovery of cheque return charges, minimum balance charges, etc. is being properly implemented.
- Scrutiny of staff accounts with abnormal /high value transactions not commensurate with the nature of account and its average balance held should be carried out to judge it in the light of AML angle or a Suspicious transaction warranting necessary reporting.
- Verification of proper reporting of CTR (Cash Transactions Report) and STR (Suspicious Transaction Report) to higher authorities in terms of AML guidelines.
- Compliance relating to Regulatory requirement of refund of fixed deposits more than Rs 20,000/- by way of Pay order or transfer to customer's deposit account and acceptance of cash deposit beyond Rs 50,000/- after obtaining PAN (from a non-customer).

Scrutiny of Exceptional transactions Report related to transactions related to deposit accounts generated from the CBS after Day End at CBS level including accounts opened and closed during the day, debits allowed against uncleared cheques, cheques returned, pre-matured withdrawal of deposits, High value deposits, etc.

Advances

The internal control in respect of advances mainly focuses on documentation and reporting of every activity involved in the process from obtaining application for a loan, till it is sanctioned, disbursed and monitored. The various activities involved in the loan process include:

- Credit Appraisal.
- Credit Sanction.
- Pre-Sanction Inspection.
- Obtaining security documents.
- Creation of equitable mortgage (EM), if any.

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- Disbursement as per the bank sanction letter
- Post Sanction Inspection.
- Credit Monitoring.

The loan product and the constitution of the borrower by and large will determine the documentation to be obtained and the checkpoints of internal control.

In the case of non-fund-based advances like bank guarantee, letter of credit, forward booking, etc. internal control should also ensure the proper exercise of delegated powers of administrative hierarchy. The reversal of expired bank guarantees and letters of credit from the books is an onerous task to be followed meticulously at the branch level.

The internal control framework should encompass a reporting framework to ensure that the credit monitoring process is meticulously followed. Credit monitoring involves continuous follow-up and management of recovery of loans. The framework as designed by the RBI in respect of identification and reporting of delinquency of loan accounts and categorization of it under SMA-0, SMA-1, SMA-2 should be followed. The early warning signals of diversion of funds, weakness in account operation, dilution in revenue of borrower, industry and market risk of borrower, Quick Mortality accounts, Advances involving Fraud element, Willful defaults, upgradation/ degradation of NPA accounts etc. should be properly addressed as a part of the internal control framework in credit monitoring.

Internal control mechanism in respect of Accounts which have been settled/ closed under Bank's Compromise Settlement schemes and recovery of decreed accounts to be monitored in terms of Bank's circulars.

The Early Warning Signals in the High-Risk Exposure Advances should be reviewed on a regular basis as the Credit Monitoring Mechanism by the Banks. These warnings may be Financial, Operational or Behavioral. Some examples of such Early Warning Signals are: - Decline in Key Business numbers, Negative or NO GST filings, Diversions, Unit or branch closure, Disputes amongst promoters, Avoidance in Lender Communications etc.

Support Functions

There are many support functions involved in the banking sector to enable seamless functioning. A comprehensive internal control procedure in the following support functions should be in vogue:

- RTGS/ NEFT, Electronic fund transfer mechanism, IMPS, SWIFT, fund, BHIM, UPI, etc.
- ATM/ CDM Services.
- Credit cards, debit cards, and gift cards issued to customers.
- Government business like handling of PF accounts, pension accounts, collection of taxes like GST/Income Tax, etc.

Regulatory Compliance

The banking sector in India is set to strict surveillance and monitoring by the Reserve Bank of India. Many reports/returns are required to be submitted to RBI periodically from various perspectives of overall monetary control. Regulatory compliance and internal control are to be interlinked. The internal controls of the bank are to be more focused on accuracy and timeliness of the submissions of such reports. The periodical reports furnished to RBI/ tax authorities/ FIU/ other regulators from the bank based on figures collected from the branches include:

- The A1 and A2 reports regarding the foreign exchange purchased and sold.
- The Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR)
- The NPA reports and the provisions coverage ratio.
- The cash balance, demand and time liabilities balance etc.
- The pending transaction report under foreign currency for LC/Bills etc.
- XOS (Export Followup Report) reports for import/ export/ bills/ remittance pending at every interval.
- Compliance related to CTR/STR reports.
- AML and KYC related compliance.

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- Compliance related to deduction and payment of taxes like Payment of TDS on interest on deposits and other payments, including filing of Forms like Form 60, Form 15G, Form 15H, etc.
- Compliance related to GST like collection of GST on various types of service charges and sending of information relating to Input Tax Credit to Controlling office, etc.
- Compliance related to Customer Service Regulations like exchange of soiled notes, etc.
- FEMA and FCRA compliance with branches handling foreign exchange Business.

System Controls

In the advent of computerization and reliance placed on the system by the banks, it is important that internal controls are tamed to protect the data integrity, data security and data process. The system controls can be enumerated as follows:

- The access control mechanism embedded within the system for logical control and physical controls outside the system should be streamlined.
- The input and output control should be properly designed. documented and audit trails in respect of changes in master records should be maintained.
- The authority levels for creation, modification, addition and deletion of data should be designed through a control matrix within the system.
- The exceptional reporting platform should be robust.
- The “*whistleblower*” system should work as desired to ensure efficient management of exceptions/deviations.
- The documentation of transaction vouchers prepared manually and punched into the system should be properly designed and structured to ensure the concept of maker checker, authority level, etc.
- The “range checks” of data should be embedded into the system.

Internal Control, Inspection and Internal Audit

- A proper backup mechanism should be ensured for seamless data flow and Business Continuity Planning (BCP).

The banks by large have all the above controls in place designed in the CBS platform. The auditor is expected to see the compliance and adherence to the set protocols.

House Keeping

The various aspects to be covered in the internal control of housekeeping of the branch include:

- The custody maintenance and use of security stationery like FD receipts, cheque books, DD leaves, stamps, etc.
- Ensure proper safety of assets and computer systems from being misused or abused.
- The upkeep and maintenance of telecommunication and the network cables to protect it from physical damage, tampering, etc.
- The safety aspects include protection from fire and other short electrical circuits, etc.
- Proper availability and functioning of CCTV (and its back up of recordings), fire alarms, emergency alarms, etc.

Inspection

The inspection process in the banks is structured and regulated by the head office or central office of the bank and as per the circulars of the RBI. The various vertical offices at the head office will concurrently inspect the branch's functioning and monitor the transactions of the branch on a regular basis.

The inspection in vogue in the banking sector includes:

- Inspection of Foreign exchange transactions by the treasury department.
- Review and renewal of loans by the regional office, zonal office, etc.
- Purchase/ Sale of Fixed assets by the premises department.
- Inter-branch reconciliation by the respective department.
- System control by the IT department, etc.

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The framework of inspections also includes various control reports, peer-to-peer inspections, inspection by the regional office and zonal office etc. The Reserve Bank of India also conducts regular inspections at the branch as well as at the head office of the bank every year called the “Annual Financial Inspection (AFI)”.

The inspections may be carried out as a regular one or surprise inspection to ensure better discipline to examine the compliance of various policies.

Internal Audit

The internal audit function of the bank includes:

- Concurrent Audit
- Revenue Audit
- Credit Audit
- Stock and Receivable Audit
- Risk based Internal Audit
- Information System Audit
- Forensic Audit
- Legal Audit
- SNAP Audit

Concurrent Audit

The Reserve Bank of India issued circular DBS.CO.ARS.No.BC.2/08.91.021/2015-16 dated July 16, 2015, and DBS.CO.ARS.No.BC.01/08.91.021/2019-20 dated September 18, 2019, on Concurrent Audit system. The scope of work to be entrusted to concurrent auditors, coverage of business/branches, etc. is left to the discretion of the head of internal audit of banks, with the due prior approval of the Audit Committee of the Board of Directors (ACB)/Local Management Committee (LMC) in case of foreign bank branches) of the bank. The RBI has stipulated that all scheduled bank in India should cover 50% of the advances and 50% of the deposit of the bank. The number of branches should also be covered periodically in rotation under the concurrent audit system. The banks are also advised to cover

Internal Control, Inspection and Internal Audit

the following specific types of departments/ branch/ offices under concurrent audit:

- High risk rating branch as per RBIA.
- All specialized branches and Large, Very Large, Exceptionally Large, and Mid-Corporate Branches.
- Treasury branches covering international and domestic treasury operations.
- Critical head office departments.

The concurrent audit as the name indicates aims at concurrent verification, prevention and detection of error frauds. The efficiency of the concurrent audit is monitored by the head office inspection department and RBI on a regular basis.

It is aimed at shortening the interval between occurrence of the transaction and verification/examination of the same by the independent person.

Revenue Audit

The audit focuses on the Income and Expenditure of the banks with special thrust to income and expenditure of banking business like interest on deposits, interest on advances, processing charges, inspection charges, folio charges, cheque book charges etc. The scope of revenue audit at present is diluted as most of the income and expenditure of banks are system driven through CBS platform without any manual intervention. However, in exceptional situations like waiver of charges, reduction of interest rates, charging of penal charges, collection of lockers rent, etc. even now holds good as the scope of revenue audits.

Credit Audit

The RBI vide circular no. (RBI/2014-15/18UBD.CO.BPD.(PCB).MC.No.9/12.05.001/2014-15 dated July 1, 2014 and Master Circular UBD.BPD.(PCB).MC.No.9/12.05.001/2013-14 dated July 1, 2013 has stipulated that the bank should frame a policy for conduct of a credit audit for every large exposure. The credit audit covers the exposure and the loans sanctioned to borrower or group of

borrowers to ensure compliance of procedures including documentation of sanction and disbursement of the loans. The credit audit also encompasses the comprehensive and critical analysis of the risk factors of a particular exposure including credit risk, market risk, operational risk.

Stocks and Receivable Audit

This audit is introduced to verify and ensure that the availability and value of stock offered as primary security against the loans is proper, adequate and enforceable. The elaborate comments and nuances on stock and receivable audit are given in a separate chapter in this Manual.

Risk Based Internal Audit (RBIA)

The RBI vide circular no. DBS.CO.PP.BC.10/11.01.005/2002-03 dated December 27, 2002, and RBI/2020-21/88 Ref.No.DoS.CO.PPG./SEC.05/11.01.005/2020-21 dated February 03, 2021, has introduced the concept of Risk Based Internal Audit to ensure a reasonable assurance about the risk management and control framework of banking operations. The effectiveness of implementation and adherence to risk management policies will be focused in this audit. The RBIA report would guide the top management and the Boards of the banks for taking appropriate decisions. The RBIA is concluded by awarding a risk rating to the branch which will act as a synopsis of the overall risk standing of the branch. ICAI has also issued Technical Guide on Risk based Internal Audit in Banks in 2024.

Information System Audit

This audit focuses on the efficiency of policy and procedures involved in the functioning of various hardware, software and telecommunication networks in the banking operations. This covers the technical aspects of data traffic, bandwidth management, logical controls, access controls etc. This is a specialized function to be conducted by experts having distinct knowledge and expertise in IS audit.

Forensic Accounting and Investigation

Forensic audit refers to in-depth verification of financial records aiming at the origination and creation, authorization and modification of any data by any individual or group of people with a preconceived objective of detecting frauds and errors. Forensic accounting and investigation is particularly done to establish the legal background of consolidating the proof and documents to be produced before any court of law to substantiate the evidential value. Mostly forensic audit is conducted in the event of fraud, embezzlement or any financial misappropriation. This audit is also conducted by specialized professionals who have experience in the field.

Legal Audit

The RBI vide circular no.2012-13/524/DBS.FrMC.BC.No. 7/23.04.001/2012-13 dated July 07, 2013 has directed the banks to frame a policy to conduct a separate legal audit of all documents and title deeds by legal experts, to ensure the availability, adherence, compliance, sufficiency and legality of the documents obtained for the loan exposure as per bank policy. The legal audit will cover the comprehensive analysis of all documents connected to a loan sanction. This is aimed at protecting the interest of the banks as a lender in the event of initiating legal action to recover the loans by enforcement of the securities offered. The legal audit should be conducted as per the policy of the Bank. The periodical verification and analysis of documents also is covered in the legal audit.

SNAP Audit

This refers to verification of certain specific transactions, aspects or documents for the understanding of their sanctity for the top management to take appropriate decisions on any lending proposals.

PART II

Domain of Concurrent Audit

Chapter 1

Evolution and General Guidelines of Concurrent Audit

Introduction

- 1.1 Concurrent audit has evolved significantly over the years, adapting to advancements in technology, changes in regulatory frameworks, and the increasing complexity of business operations:
 - (i) Traditional Audits: Initially, audits were conducted with a focus on transaction verification rather than risk assessment.
 - (ii) Integration of Technology: The introduction of core banking solutions allowed auditors to access real-time data for analysis in read only formats.
 - (iii) Risk-Based Auditing: Focus of Reserve Bank of India shifted from mere compliance checks to identifying key risks and mitigating them proactively.
 - (iv) Continuous Monitoring: Today's concurrent audits are integrated into business processes, providing ongoing oversight instead of periodic evaluations.
- 1.2 Evolution of concurrent audit in banks may be explained as follows:
 - (i) Reserve Bank of India vide its Circular of October 1993 introduced the system of Concurrent Audit.
 - (ii) Initially it was in existence for Large and exceptional Large Branches.
 - (iii) This measure of the Reserve Bank of India (RBI) arose out of the recommendations of the *Ghosh Committee on frauds and Malpractices in Banks*.
 - (iv) In its said circular, the banking regulator explained concurrent audit as being "an examination which is contemporaneous with the occurrence of transactions or is carried out as near thereto as

Evolution and General Guidelines of Concurrent Audit

possible. It attempts to shorten the interval between a transaction and its examination by an independent person.”

- (v) The primary objective of the introduction of a formal system of concurrent audits in banks is to examine the transactions at its occurrence and errors, irregularities to be corrected immediately. The serious irregularities or fraud indicators to be reported immediately.
 - (vi) The RBI circular also clarified that concurrent audit is essentially a management process.
 - (vii) The importance of concurrent audit was highlighted by the banking regulator as being essential for:
 - Sound internal accounting functions.
 - Effective controls.
 - Setting the tone for vigilance internal audit to preclude incidence of serious errors and fraudulent manipulations.
- 1.3 RBI has issued circular on Concurrent Audit System from time to time, last circular issued vide Reference No RBI 2019-20/64 DBS. CO.ARS. No.BC.01/08.91.021/2019-20 dated 18th September 2019. As per the circular the scope of the concurrent audit is to be decided by the banks with prior approval of Audit Committee of the Board of Directors.
- 1.4 Banks are advised to identify the risk sensitive areas in their business models, and it shall be covered under Concurrent Audit.
- 1.5 The Concurrent Audit Coverage depends upon Risk Assessment of a Unit and shall cover the large number of transactions for verification.
- 1.6 Banks are advised to conduct the Annual Review of the effectiveness of concurrent audit system and performance of the Concurrent Auditors.
- 1.7 The said circular has mandated that in case of detection of fraudulent transactions it should be reported immediately to the Head of Internal Audit Department, Chief Vigilance Officer and concerned branch manager (if branch is not involved).

Appointment of Auditor and its Accountability in Terms of RBI Guidelines

1. The Reserve Bank of India vide circular DBS.CO.ARS. No. BC. 01/08.91.021/2019-20 dated September 18, 2019 provides as follows in respect of the appointment of a concurrent auditor:
2. This RBI Circular is applicable for All Scheduled Commercial Banks (other than Regional Rural Banks), Small Finance Banks, Payments Banks and Local Area Banks.
3. This Circular is issued after circular DBS.CO.ARS. No.BC.2/08.91.021/2015-16 dated July 16, 2015 on 'Concurrent Audit System in Commercial Banks - Revision of RBI's Guidelines'. RBI issued Master Circular on Inspection & Audit Systems in Primary (Urban) Co- operative Banks vide RBI/2015-16/3/ DCBR.CO.BPD. (PCB)MC. No. 3/12.05.001/2015-16, July 1, 2015.
4. Concurrent audit aims at shortening the interval between a transaction and its independent examination.
5. Concurrent audit is:
 - (a) An integral to the establishment of sound internal accounting functions and effective controls.
 - (b) Regarded as part of a bank's early warning system to ensure timely detection of serious errors and irregularities.
 - (c) Helps in averting fraudulent transactions and preventive vigilance in banks.
6. RBI prescribed Guidelines for scope, coverage of business/branches, minimum items of coverage to Concurrent auditor of banks from time to time. Due to the differing levels of centralization in banks, diverse nature of activities undertaken by various banks and commencement of operations by small finance banks and payments banks, a common programme of work for concurrent audit applicable to all banks may not be desirable.
7. The Expert Committee, headed by Sri Y.H. Malegam, past President of the ICAI which was appointed by RBI, initially in the year 2010, has made certain recommendations in Concurrent Audit.

Guidelines of Concurrent Audit

The existing guidelines on the subject have, therefore, been reviewed and the revised guidelines given as under:

A. Coverage

- a. With the prior approval of the Audit Committee of the Board of Directors (ACB) / Local Management Committee (LMC – In case of Foreign Banks) of the respective Banks must decide on the following matters:
 - i. Scope of work entrusted to Concurrent Auditors.
 - ii. Coverage of Business/branches.
 - iii. Other areas of Concurrent Audit.
- b. Based on the risk sensitive areas identified by the Banks, specific Business Models must be covered under Concurrent Audit.
- c. ACB/LMC must decide and determine the detailed scope of Concurrent Audit.
- d. Concurrent audit coverage shall be based on the identified risk of the unit.
- e. Concurrent audit coverage must include random transaction testing, by way of sufficiently testing Large Sample of the Transactions.
- f. Minimum areas of coverage as per the RBI Circular are given below:

- | |
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| <ol style="list-style-type: none">1. Cash transactions including physical verification of cash, etc.2. Loans & Advances including physical verification of securities, delegation of Powers for sanction, Security Charge Creation, end use verification of funds, monitoring of accounts with excess drawings, monitoring of projects, etc.3. Adherence to KYC / AML guidelines including monitoring of transactions in accounts, compliance with Foreign Account Tax Compliance Act (FATCA) and Common |
|--|

Reporting Standards (CRS), monitoring of transactions in new accounts/staff accounts, reporting of CTR/STR, etc.

4. Remittances/ Bills for Collection including SWIFT transactions, monitoring of overdue statements (bills purchased / discounted / negotiated, etc.).
5. House Keeping including reconciliation of accounts, monitoring of General Ledger/Subsidiary General Ledger/Parking Accounts, opening of internal accounts, etc.
6. Treasury operations.
7. Non-fund-based business.
8. Foreign Exchange transactions.
9. Clearing transactions.
10. Verification of Merchant Banking Business.
11. Verification of Credit Card / Debit card business.
12. Conduct of employees, mis-selling of products, etc.
13. Compliance to RBI guidelines and internal Policy guidelines issued from time to time.

- g. Care must be taken by ACB/LCB of the respective band ensure that all Centralised Processing Centres (Business Organisation and Monitoring) are covered under Concurrent Audit.

B. Appointment of Auditors

- i. At the discretion of Individual Banks, Concurrent audit should be done by bank's own staff or external auditors (which may include retired staff of its own bank).
- ii. The Head of Internal audit in the bank should participate in the section of Concurrent auditors.
- iii. He should be responsible for the quality review (including skills of the staff employed) of the work of the concurrent auditors reporting to her/him.

Evolution and General Guidelines of Concurrent Audit

- iv. In case if any partner of a Chartered Accountant firm is a Director on the Board of a bank, no partner of the same firm should be appointed as concurrent auditor in the same bank.
- v. In case the bank has engaged its own officials as concurrent auditors, they should be experienced, well trained and sufficiently senior. The staff engaged in concurrent audit must be independent of the branch/business unit, where concurrent audit is conducted.

C. Accountability

- i. Any Serious acts of omission or commission of the external firms who have been appointed as concurrent auditor are noticed in their working, their appointments may be cancelled after giving them reasonable opportunity to be heard and the fact shall be reported to ACB/ LMC of the bank, RBI and ICAI.
- ii. The bank should frame a policy for fixing accountability in cases of serious acts of omission or commission noticed in the working of bank's own staff or retired staff, working as concurrent auditors.

D. Tenure

- i. The Maximum Tenure of External concurrent auditor with the bank shall be decided by ACB/MLC.
- ii. The tenure of External Concurrent auditor with a Bank shall not be more than" 5 years on continuous basis.
- iii. No concurrent auditor shall be allowed to continue with a branch / business unit for a period of more than 3 years.
- iv. The age limit for retired staff engaged as Concurrent Auditor may be capped at 70 years.

E. Remuneration

- i. ACB/LMC of the bank shall decide the remuneration to be paid to external concurrent auditors.
- ii. Based on the scope and coverage of audit, skill sets required, number of staff required and the time to be devoted for the audit, the Remuneration of the Concurrent auditor is fixed by ACB/LMC.

F. Review of effectiveness of Concurrent Audit

- i. ACB/ LMC of the bank should review the effectiveness of the Concurrent Audit system as well as the performance of the concurrent auditors on an annual basis and take necessary measures to suitably strengthen the system.

G. Reporting System

- i. Banks' Internal Audit Department should develop a reporting system for concurrent auditors with the approval of ACB/LMC.
- ii. The findings of the concurrent auditors may be received in a structured format prescribed by the bank.
- iii. Minor irregularities pointed out by the concurrent auditors shall be rectified on the spot. The major deficiencies/aberrations noticed during audit should be immediately brought to the notice of Head Office/ Controlling Office of the concerned branch/ business unit of the bank.
- iv. A quarterly review containing important features brought out during concurrent audits should be placed before the ACB/LMC. The zone-wise findings of concurrent audit may be reported to ACB/LMC on a quarterly basis.
- v. Whenever fraudulent transactions are detected, they should immediately be reported to Internal Audit Department (Head Office) as also to the Chief Vigilance Officer as well as Branch Managers concerned (unless the branch manager is involved).
- vi. Follow-up action on the concurrent audit reports and rectification of the deficiencies should be accorded high priority by the Head Office/Controlling Office of the concerned branch/business unit of the bank.

Audit Committee of the Bank

In pursuance of extant RBI guidelines, a Bank is required to constitute an Audit Committee of its Board of Directors (ACB).

- The membership of the audit committee is restricted to the Executive Director, Nominees of the Central Government and the RBI, Chartered Accountant Director and one of the non-official directors.

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- One of the functions of this Committee is to provide direction and oversee the operations of the entire audit function in the Bank.
- The Committee also should review the internal inspection/audit function in the Bank, with special emphasis on the system, its quality and effectiveness in terms of follow up.
- The Committee should review the system of appointment and remuneration of the concurrent auditors.

Training

- Considering the coverage of this audit assignment and the specialized nature of work there is also a need for training to be imparted to the staff of the auditors.
- This training should be given in specialized fields, such as, foreign exchange computerization, treasury functions, latest KYC guidelines, demat activities areas of income leakage, fraud prone areas, determination of credit rating and other similar specialized areas.
- The Bank can organize such training programmes so that it can ensure the quality of audit.

Purpose of Concurrent Audit

1.9 Purpose of concurrent audit as per the RBI Circular is as follows:

- (i) The Concurrent audit is an examination which is contemporaneous with the occurrence of transactions or is carried out as near thereto as possible.

(That means when transactions are carried out by the Bank/Branch, the same should be checked immediately within shortest possible time depending upon risk involved without any delay).

- (ii) It attempts to shorten the interval between a transaction and its examination by an independent person. There is an emphasis in favour of substantive checking in key areas rather than test checking.

(Concurrent Auditor should decide the sample size for verification of transactions as specified in the terms of appointment by the

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Bank and 100% verification of bank transactions should be carried out in high risk and sensitive areas).

- (iii) This audit is essentially a management process integral to the establishment of sound internal accounting functions and effective controls and setting the tone for a vigilant internal audit to preclude the incidence of serious errors and fraudulent manipulations.

(Concurrent audit is helpful to find the serious errors and fraudulent manipulations that will be there in a Bank).

- (iv) A concurrent auditor may not sit in judgment of the decisions taken by a branch manager or an authorized official. This is beyond the scope of concurrent audit. However, the audit will necessarily have to see whether the transactions or decisions are within the policy parameters laid down by the Head Office, they do not violate the instructions or policy prescriptions of the RBI, and that they are within the delegated authority.

(Wherever the Branch Manager deviate from the Bank HO norms, he should cover those deviations and report).

- (v) In very large branches, which have different divisions dealing with specific activities, a concurrent audit is a means to the in-charge of the branch to ensure on an ongoing basis that the different divisions function within laid down parameters and procedures.

Coverage of Business/ Branches

- 1.10 In view of significant developments in the banking sector during the past decade, it is required that new areas posing risk may be brought under the purview of concurrent audit. It is the duty of the Concurrent auditor/Banks to identify the new areas of risks in Banks.
- 1.11 Many activities/ operations are being carried out in a centralized manner at various units set up for that purpose and the scale of transactions/ operations undertaken at these units is large.
- 1.12 With a view to ensuring that the functioning of these units is as per the internal as well as regulatory guidelines and mitigating the risk associated with large-scale operations, such non-branch units may be

Evolution and General Guidelines of Concurrent Audit

brought under the purview of concurrent audit. Hence the scope of concurrent audit is more nowadays and exhaustive. All the Concurrent auditors must know the technique of doing concurrent audit with appropriate knowledge of conducting audit of banks.

1.13 While selecting the branches for concurrent audit: (from banker side):

- (i) The risk profile of the branches needs to be considered. The branches with high risk are to be subjected to concurrent audit irrespective of their business size.
- (ii) Further, all specialized branches viz. may be covered under concurrent audit:
 - Agri, SME
 - Corporate
 - Retail Assets
 - Portfolio Management
 - Treasury Operations
 - Forex Transactions
 - Funds Department
 - Asset Reconstruction Branches
 - Back Office, etc.
- (iii) Certain areas where risk has reduced on account of computerization, implementation of core banking system may be excluded from the purview of concurrent audit.
- (iv) Nowadays the scope of Concurrent audit is more due to the extensive introduction of CBS operations. There is a lot of scope for misuse of the CBS environment.

1.14 The following branches, business activities/verticals of a bank may be subject to concurrent audit:

- (i) Branches rated as high risk or above in the last Risk Based Internal Audit (RBIA) or serious deficiencies found in Internal Audit.
- (ii) All specialized branches like, Large Corporate, Mid Corporate,

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exceptionally large/very large branches (ELBs/VLBs), SME.

- (iii) All Centralized Processing Units like:
 - Loan Processing Units (LPUs).
 - Service branches.
 - Centralized account opening divisions, etc.
- (iv) Any specialized activities such as wealth management, portfolio management services, Card Products Division, etc.
- (v) Data Centres.
- (vi) Treasury/ branches handling foreign exchange business.
- (vii) Investment banking.
- (viii) Bigger overseas branches.
- (ix) Critical Head Office Departments.
- (x) Regional/ Zonal Offices (in few banks they are conducting Concurrent Audit).
- (xi) Chest Branch.
- (xii) Loan Management Branches.
- (xiii) Loan Recovery Division Branches.
- (xiv) Any other branches or departments where, in the opinion of the bank, concurrent audit is desirable.
- (xv) Concurrent audit at branches should cover at least 50% of the advances and 50% of deposits of a bank.

Scope of Concurrent Audit

- 1.15 Revised RBI circular on concurrent audit specifies following in respect of scope of concurrent audit. Types of activities to be covered under concurrent audit have been broadly given in the RBI's circular dt. 18 September 2019:
- (i) The main role of concurrent audit is to supplement the efforts of the bank in carrying out simultaneous internal check of the transactions and other verifications and compliance with the procedures laid down.

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- (ii) The scope of concurrent audit should be wide enough/focused to cover certain fraud - prone areas, such as, handling of cash, deposits, advances, foreign exchange business, off-balance sheet items, credit- card business, internet banking, etc.
- (iii) The detailed scope of the concurrent audit should be clearly and uniformly determined for the bank by the bank's Inspection and Audit Department in consultation with the bank's Audit Committee of the Board of Directors (ACB).
- (iv) In determining the scope, importance should be given to checking high- risk transactions having large financial implications as opposed to transactions involving small amounts.
- (v) While the detailed scope of concurrent audit may be determined and approved by ACB. Besides, the items where RBI has specifically advised the banks to be covered under concurrent audit, may also be part of the checklist of the concurrent auditor.

Focus of Concurrent Audit

- (i) A study of the *modus operandi* of the fraudulent transactions, generally, indicates that the processing of transactions is done without adhering to the systems and procedures.
- (ii) This permits an unscrupulous person to misuse the procedures of the bank and undertake fraudulent transactions, which remains unnoticed for a long time. Concurrent Auditor would, therefore, need to focus on adherence to laid down systems and procedures and safeguards.
- (iii) The Auditor needs to conduct this independent assessment of audit risk *vis-a-vis* the internal control in the branch while finalizing the audit programme.

Chapter 2

Concurrent Audit Universe

- 2.1 The concurrent auditor may scrutinize certain daily transaction of the branch, as per terms of the Bank and in absence of any specific guidelines, on the same day and certain others on the next working day. He may scrutinize certain items at periodical intervals and other lesser important items on any day of the month maintaining random sampling and surprise element. The concurrent auditor is, normally, required to carry out audit of transaction based on daily vouchers, general ledger balance book, subsidiary books, and ledgers.

Note: This verification of voucher intervals must clearly spell out in the Appointment letter. If it is not there, Concurrent auditor must depend on the Bank's Concurrent Audit Manual and to the verification as stated in the manual. Even if it is not there, the Concurrent Auditor can write to Bank's Appointing Authority and get the same clearly clarified. This will solve lot of issues towards your verification. Auditor may disclose methodology followed as prescribed under Standard on Auditing 530 - Audit Sampling issued by ICAI.

- 2.2 To facilitate the work of a concurrent auditor and ensure that he/they don't miss any important aspect, the checklist for audit is prepared according to the size of the branch by the auditor himself in accordance with the guidelines and instructions of the Bank. This checklist is however, normally, given by each Bank and is to be followed by the Concurrent Auditor. For preparing this checklist, one of the approaches followed is to prepare it based on items to be verified on daily basis, weekly basis, fortnightly basis, monthly basis, quarterly basis, half yearly basis and yearly basis.

Without preparing the Checklist, Concurrent auditor should not do the audit. The same Check list must be updated at least once in a quarter or as and when modification/amendment conveyed by Bank to the Concurrent Auditors, it may be based on Bank's circulars, directions. In case of change expected in the background of regulatory directions/circular, same should be highlighted and reported suitably.

- 2.3 The various items of banking transaction/services to be verified are as follows:

Deposits

- 2.4 One of the main sources of bank finance is the deposits accepted from public. To cater to the needs of various types of customers, banks offer different types of accounts with various facilities attached to these accounts.

The Bank accounts are broadly classified into the following categories:

- (i) Savings Deposit.
- (ii) Current Deposit.
- (iii) Fixed Deposit.
- (iv) Recurring Deposit.
- (v) Saving cum fixed deposit/Swift A/C.
- (vi) Non-resident Account; etc.

(i) Savings Deposit Account

The Savings Deposit Accounts are opened to attract small savings of the public. The number of withdrawals per year is, normally, restricted. A Savings Deposit cannot be opened by any trading or business concern, whether it may be individual, or partnership concern, etc. A bank may open savings deposit account for the primary cooperative credit society which is financed by that Bank. No overdraft is, normally, allowed on Savings Account, except Pradhan Mantri Jan- Dhan Yojana (PMJDY).

The following Few persons are entitled to open Savings Deposit account in a Bank:

1. An individual in his/her name.
2. More than one individual can jointly open Savings account.
3. Minor represented by Guardian.
4. A minor himself/ herself provided he/ she attained the age of 14 years.
5. School going Minor Children above the age of 12 years.
6. An Illiterate person.

7. A Blind Person.
8. Clubs, Association (whether registered or not), Charitable and Religious Institution, Trusts, Local Bodies, Primary Cooperative Bank, as permitted by RBI.

(ii) Fixed Deposit Account

- Fixed Deposits, named differently by Banks, are the funds kept by the public with the Bank, which are not required immediately and are repayable on demand or on the expiry of term of the deposits.
- The period of deposits may vary from 7 days to 5 years or even more than 5 years.
- The rate of interest varies depending on the period the deposit is kept and certain other parameters as decided by the banks, like, Senior Citizens/ retired staff.
- However, the benefit shall not accrue to staff other than retired/ superannuated unless the bank specifically mentions.
- Sometimes large value deposits are given special rate of interest by the banks, but interest rate can be fixed based on Bank's Head office directives.
- Premature of Deposits are also allowed in case of Fixed Deposits.

Classification of Deposits

For the purposes of the disclosures in the Balance Sheet, the RBI classifies the deposits accepted by Bank into following categories, namely:

- I. Demand Deposits.
- II. Savings Bank Deposits.
- III. Term Deposits.

I. Demand Deposits

- (i) From Banks Includes all Bank deposits repayable on demand.
- (ii) From Others Includes all demand deposits of the non-Bank sector. Credit balances in overdrafts, cash credit accounts, deposits payable at call, overdue deposits current accounts whether

inoperative or not, matured term deposits, and cash certificates, certificates of deposits, etc. are to be included under this category.

II. Savings Bank Deposits

Includes all savings Bank deposits (including inoperative savings Bank accounts).

III. Term Deposits

- (i) From Banks Includes all types of Bank deposits repayable after a specified term.
- (ii) From Others Includes all types of deposits of the non-Bank sector repayable after a specified term. Fixed Deposits, cumulative and recurring deposits, cash certificates, certificates of deposits, annuity deposits, deposits mobilized under various Term based schemes, foreign currency non-resident deposit accounts, etc. are to be included under this category.

Notes:

Deposits included under demand deposits as per RBI classification are:

- (i) Credit balance in overdrafts and Cash Credit accounts.
- (ii) Deposits payable at call.
- (iii) Overdue deposits.
- (iv) Inoperative current accounts.
- (v) Matured term deposits and cash certificates.
- (vi) Certificates of deposits, etc.

The cash credit account would be included if the balance is showing credit balance. The current accounts are also payable on demand. The outstanding demand drafts is also to be included under the demand deposit head.

Term deposits as per the classification would include:

- (i) All deposits repayable after a specified term.
- (ii) Fixed deposits.
- (iii) Cumulative and recurring deposits.

- (iv) Cash certificates.
- (v) Certificates of deposits.
- (vi) Annuity deposits.
- (vii) Deposits mobilized under various schemes.
- (viii) Ordinary staff deposits.
- (ix) Foreign currency.
- (x) Non-resident deposit accounts, etc.

Advances

- 2.5 The lending of funds to customers is the main business of a banking company. A bank earns income from the interest and discount, etc. arising out of the funds lent by it. The lending of funds has inherent risks, i.e. the loan or advance may go bad.

Banks, therefore, follow prudential lending principles as prescribed by the Reserve Bank of India and Bank's internal policy guidelines while lending the funds in order to reduce the associated risks.

Various Forms of Credits

The advances made by banks are, normally, in the following forms:

- (i) Cash Credit
- (ii) Overdraft
- (iii) Loans

Cash Credit

- Cash credit is an arrangement between a bank and the customer by which money is advanced against hypothecation of stocks in trade, book debts and a bond of credit by one or more sureties.
- The borrower can reduce the debit balance by paying back surplus available with him and redraw the amount as and when needed.
- The interest is charged on the amount utilized.
- In certain cases, commitment fee is charged for non-utilisation of arrangement as agreed.

- Cash credit is, normally, sanctioned by the bank for a period of one year and is, generally, renewed if the account is operated satisfactorily.
- The cash credit is generally secured by tangible assets.
- The borrower need not withdraw the whole amount and may withdraw the funds as and when required.
- The maximum amount sanctioned depends on the working capital requirements of the borrower.
- The interest is charged monthly on the outstanding debit amount to the debit of the borrower's account.
- The asset created out of Cash Credit account is called as "Primary Security" and is taken as part of Cash Credit Loan's Security Value.
- Non-renewal of limit will attract Penal charges Penal charges till it is renewed.
- Insurance of stocks plays a very vital role in Cash Credit account.
- In Cash Credit Limits, submission of Stock statement and Credit Statement is compulsory to arrive at the Drawing Power.

Overdraft

- The overdraft, unless the nomenclature is used by some Bank for certain type of withdrawals of secured/unsecured type, is a facility given by a bank to the temporary needs of the borrower.
- An overdraft facility is usually sanctioned against securities like shares, stock, bonds, Bank's own fixed deposit receipt, Govt. Securities, like, NSC, life insurance policy (surrender value), immovable property, etc.
- Submission of Stock statement and Debtor Statement can be done once in a year, as per the Sanction terms and conditions, provided the loan is sanctioned for the purpose of business.
- Overdraft Loan is required to be renewed every year, but the renewal of Overdraft depends on the conditions stated in the Sanction Letter.

Loan

There are Two Types of Loans:

- (i) Demand Loan
- (ii) Term Loan

- A demand loan is repayable on demand/called back from the bank. A loan which is repayable within 3 years is called a short-term loan.
- Loans repayable within a period of 3 to 5 years are called medium term loans.
- Loans repayable beyond 5 years are long term loans.
- Sometimes loans are disbursed over a period depending on the requirement of the borrower.
- The interest is charged on the amount disbursed as reduced by the repayment, if any, on daily outstanding balances.
- Auditor should ensure end use of the funds irrespective of the loan disbursed in lumpsum or in stages and see to it that, the funds are remitted to the bank account of supplier/seller of goods or services. The repaid amount is not allowed to be redrawn even if it is by way of prepayment.

Loans can be either secured or unsecured:

- An unsecured loan is one for which the bank holds no security other than the personal guarantee of the borrower. Such loans are now an uncommon feature except personal loans.
- A bank also extends term loans for the purpose of purchase of assets.
- The repayment is fixed in term loan by way of instalments.
- When only a part of the advance is covered by securities as at the date of balance sheet, that part should be classified as secured and the remaining amount be shown as unsecured.
- Banks do not advance amounts equal to the value of the security but keep appropriate margin to provide for a decline in the value of security.

- RBI also directs from time to time, specified margins to be kept against some securities like Shares/ items of essential use, etc.

A commercial bank's performance is evaluated mainly on the quality of its housekeeping and proper functioning of its large network of branches. Numerous transactions involving huge sum of money take place every day at bank branches.

The accounts of everyday transactions of a branch are prepared and reconciled every day.

Any mistake/wrong accounting leads to enormous representation of true situation of the branch to its controlling/head office. Any mistake in paying interest to the depositors and or realizing interest from the borrower's leads to revenue leakage in the banking sector.

There have been rapid changes in the lending activity undertaken by banks, marked by:

- Deregulation of interest rate.
- IRAC norms, i.e., Income Recognition and Asset Classification.
- Stricter Provisioning and Capital Adequacy norms.
- Introduction of Risk based Management System.
- Lending through Cash Flow System in addition to MPBF System (Maximum Permissible Bank Finance).

In today's banking, the role of a bank can be stated to be three-fold as under:

- (i) To make a proper selection of borrower, who is worthy of bank's assistance, both in terms of commercial principle and as well as the national priority.
- (ii) To ensure that funds lent is safe; and
- (iii) To ensure that good and proper use of bank credit is made by the borrower, judging from two angles - first, bank credit is not pre-empted because of inefficient working capital management, speculative build-up of inventory and secondly, bank credit is not diverted for "unauthorized use".

Undue emphasis of safety of funds, is however, not desired by the

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banking sector nowadays, since, if the advance is mis-utilized, i.e., used for the purpose' other than the originally intended one, it attracts comments notwithstanding safety of the same.

Safety of advance does not merely depend upon the availability of security of adequate value; it is also based upon continued viability of the enterprise, because, if the enterprise is weak, it is extremely doubtful whether the security would fetch the value originally ascribed to it.

It is quite clear from the foregoing that concept of safety of funds in banks has changed, as it should, because no longer the banker does perform the role of a moneylender but finances an economic activity and thus security is simply not synonymous with safety.

While discharging the duties of professional assignments entrusted by the banks, the concurrent auditor should, investigate the aspect of supervision and follow-up of bank credit to protect the interests of the Bank.

The broad aspects which may be investigated are enumerated below:

- (i) To see compliance with the terms and conditions of the sanction (essence of credit audit to be taken into consideration).
- (ii) To undertake physical inspection of godown/ factory, only if specifically desired by the Bank.
- (iii) To observe continued viability of operations.
- (iv) To verify the end use of bank credit.

(A) General Information About Terms Loans

- (a) Term Loan is sanctioned for various purposes. Main categories of term loans and other types of finance are given hereunder. Banks have developed various products for business, personal, agricultural loans. For specific information about the loan scheme, auditors should study the schemes of the particular banks.

Retail / Personal Loans

- Home loans and loans against property or mortgage loans
- Vehicle/automobile loans
- Education loans

- Personal loans
- Consumer durable loans
- Micro Finance loans
- Jewel loans or gold loans
- Loan against securities
- Mudra loans

Large / Medium / Small Corporates / Business Loans

- Term Loan for Land & Building, Plant & Machinery
- Industry specific finance schemes
- Term Loans to NBFCs / MFIs
- On lending
- Term Loans for Infrastructure Projects
- Rent Discounting Loans
- Asset Backed Loans
- Equipment Finance
- Corporate Loans
- TREDS (Trade Receivables E-Discounting Scheme)
- Supplier Credit

Forex Loans

- Pre-shipment finance (Packing Credit)
- Post-shipment finance (Bills Discounting)

Agriculture Loans

- Short Term Loans (Farm Credit / Crop Loans)
- Kisan Credit Cards
- Gold Loans for Agriculture
- Loans to Self Help Groups
- Medium Term Loans (Purchase of equipments)
- Long Term Loans (Purchase of Land)
- Loans to Agro Processing Industries / Agri Allied Activities
- Loans under Prime Minister Atmanirbhar Schemes
- Loans to Agri Clinics & Agri Business Centers

(b) Term Loan should be repaid on the following methods:

(A borrower should repay the loan as per the terms and conditions mentioned in the Loan Sanction Letter).

1. Principle per month (Loan amount sanctioned / No of months due) + Interest (as and when debited) per month.
2. Equated Monthly Instalments (EMI).
3. Holiday Period Interest + Method 1 or Method 2.
4. Bullet Repayment Method.
5. Balloon Repayment Method.

Financial Follow Up

- (a) The financial follow-up devised by Chore Committee is an off shoot of RBI's concern on lack of proper follow-up procedures then prevalent in commercial banks.
- (b) For such financial follow up the Chore Committee suggested certain Quarterly Information System to be provided by the borrowers to enable the bank to verify as to whether borrower's operating performance and finance management conform to the budget and promise made to the bank while availing the bank credit.
- (c) This has been replaced by QMR/HMR Statement.

The concurrent auditor, while discharging his duties, should have knowledge of such follow-up statements as well as how they should be scrutinized to protect the interests of the bank.

It is mandatory under the RBI regulations for a limit above a specified amount but below the cut-off point has been left to the discretion of the banks.

Particulars of QMR/HMR (which are now in use) replacing QIS are given below:

Description	Periodicity	Date of Submission
QMR I replacing QIS II	Quarterly	Six weeks after the Close of the Quarter to which it relates.

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HMR I replacing QIS III	Half Yearly	Two months from the commencement of the half year to which it relates.
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Note: Non submission HMR statement, on time, as per sanction letter attracts Penal charges Penal charges to be payable by the borrower.

Credit Cards

The credit card operations occupy a special place in the modern-day banking industry. A credit card has three important functions:

- It is an instrument of paying for goods and services.
- It is an instrument of obtaining cash.
- It is a source of revolving credit. Usually, there is a contract between the card issuer (the Bank) and the card holder(customer) whereby – the card holder is permitted to make use of the card at specified retail outlets (known as member establishments) to pay for the goods and services.

The mechanism of a credit card can be illustrated as follows:

- As soon as the card holder makes purchases from specified retail outlets/member establishment, the retail outlets make out bills to the account of the card holder and obtains payment from card organizations like Visa or Master immediately who in turn makes a bill to the Bank which issued the card.
- The Bank makes payments to Visa or Master immediately.
- Subsequently, the payment is realized from the respective card holder.
- RuPay Card has been introduced in 2015 as an economic option and is being used, particularly, for Pradhan Mantri Jan-Dhan Yojana (PMJDY) scheme although not restricted for the scheme.

RBI has issued Master Direction – Credit Card and Debit Card – Issuance and Conduct Directions, 2022 RBI/2022-23/92 DoR.AUT.REC. No.27/24.01.041/2022-23, April 21, 2022, which are updated as on March 7, 2024.

Types of Cards

There are many types of cards in the Indian market and the more popular are listed below:

A. Credit Card

- (a) It is an instrument of payment which enables the cardholder to obtain either goods or services from merchants where arrangements are made to reimburse the merchant.
- (b) The outstanding amount is payable by the card holder to the bank over a specified period which carries a specified rate of interest also.
- (c) Delay in payment of Credit Card attracts Penal charges Penal charges.

B. *Default in credit payment will have direct impact on "Credit Information Companies" like CIBIL, Transunion, SMERA, etc. score of the Borrower.*

C. Debit Card

- (a) It is a payment card used to obtain cash, goods and services by automatically debiting the payments to the cardholder's Bank account immediately.
- (b) For this, the card holder must have a credit balance in accounts where the card pertains.
- (c) Payment under the Debit card will be made by the customer only when he/she has got credit balance in the account and the default have no effect on the accounts as the supplier of goods or services will not deliver the goods as "no payment received".

Co-branded cards

- (a) Co-branded cards are those that a bank promotes jointly with other non-financial institutions.
- (b) Card holders use their cobranded cards in the same way as they use any other cards but each time they make a purchase, they accumulate points which enable them to claim a discount in the price.
- (c) Note: At the End of this Chapter 2 Part II, FAQ issued by RBI regarding "Card Transactions" are reproduced. (Courtesy RBI).

Frauds in Card Transaction

- (a) Wrongful use of lost and stolen card is the biggest area of fraud.
- (b) Credit cards are sometimes picked up by unscrupulous persons and

they use the cards indiscriminately before steps can be taken to hot list the cards by the issuing banks.

- (c) Credit card issuing banks now shifted to technology-based control and monitoring to save user from fraudster by allowing to set limit on nature and type of the transactions executed vide credit card.
- (d) Lot of Frauds took place in International Debit/Credit Cards. As on Auditor one must see the nature of Frauds and the result of handling those types of frauds.

Foreign Exchange Transactions

Branches dealing in foreign exchange are classified in three categories:

- The “A” categories are allowed to open and maintain currency-wise account with foreign banks/correspondents. These accounts are called Nostro accounts.
- While “B” category branches operate directly upon the account (Nostro accounts) opened by “A” category branches.
- The “C” category branches can handle foreign exchange business only through “A” and/or “B” class branches.
- The banks authorize some branches only to deal with spot or forward sale/purchase of foreign currencies with RBI, foreign correspondent banks, other banks in India.
- Foreign banks are allowed to open accounts with Indian banks for foreign exchange dealings. These accounts are called Vostro accounts.
- Indian Banks are allowed to open Bank accounts in foreign country in that country’s currency account and that account is called as “Nostro Account”.
- Foreign Banks are allowed to open its account India in Indian rupee to carryout foreign exchange transactions. That type of account is called as “Vostro Account”.
- All the foreign exchange business transactions are governed by the Foreign Exchange Management Act (FEMA), 1999.
- A bank must be very careful in dealing with foreign exchange transactions because it must have full knowledge about foreign parties.
- The bank must take care that the transaction does not violate the

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provisions of FEMA, and the rules framed there under.

- The foreign exchange rate fluctuation is another hazard in these dealings and may involve loss.
- The bank scrutinizes the documents, shipping bills and orders, etc. received from the customers and makes independent assessment of customers' standing and ability to meet the commitments.
- The banks enter forward sale/purchase of foreign currency to protect their dealings in foreign exchange.
- The forward sale/purchase transactions would cover spot or forward purchase of foreign currencies.

The concurrent auditor must investigate the following factors involved in foreign exchange dealings of banks:

- (i) Compliance with FEMA.
- (ii) Compliance with RBI rules.
- (iii) Follow-up of procedures of authorized dealers.
- (iv) Brokers' notes.
- (v) Reconciliation/correspondent statements of Nostro accounts balances are to be reconciled with corresponding accounts.
- (vi) Interest applicable on credit/debit balance on Nostro accounts and profit/loss on exchange accounts to be recorded in profit and loss account.
- (vii) In the case of Nostro accounts, because the debits are raised later, on account of payments made of TTs/MTs/DDs drawn on Indian banks by foreign banks/exchange houses, etc. the interest loss can be avoided if the debts are value dated.
- (viii) Overdrafts allowed in Nostro accounts.
- (ix) Reconciliation of daily closing balances with accountholders and confirmations obtained.
- (x) Maintenance of the Registers as per the requirements of RBI.
- (xi) Submission of periodical returns to RBI.

The various statements to be filed by banks are as follows:

- (i) Weekly return of various currencies held in different forms and monthly returns of bid bonds, guarantees issued, statement of non-resident accounts, export letters of credit, blocked accounts.
- (ii) Fortnightly returns of export bills negotiated/sent for collection; outward remittances effected against imports sale/purchase transactions in foreign currencies.
- (iii) The details regarding purpose, commodity, country, currency, terms of payment, etc.
- (iv) Statement of overdue export bill awaiting realization, purchases in the form of travellers' cheques, currency notes and gift parcels exported every quarter.
- (v) R>Returns are being submitted regularly by the branches to RBI who are dealing directly foreign exchange transaction (either purchase or sale of foreign currency) on behalf of that branch or other branches.

Dealing Limits

The guidelines for dealing limits are discussed below:

Daylight Limits

- The Exchange Control rules requires that the position should be square or near square in each currency at the close of business each day.
- During operations, during the day both with customer as well as in inter-Bank business, the dealer may have to maintain open positions in the various currencies transacted by the bank.
- The management should, therefore, lay down the maximum position limits in each currency that may remain uncovered during the day after a careful study of the nature and volume of operations (customer as well as inter-Bank) at each centre at which the bank undertakes inter-Bank operations and the conditions of the exchange markets, generally, both in India and abroad.
- This necessitates a periodical review (in some circumstances even daily reviews) of the maximum daylight positions permitted to the dealer(s).
- The need for returning the position to square or near-square is stressed while laying down daylight limits, as the exchange market conditions, or

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the inadequate trading hours or time zone factors make it difficult for the dealer(s) to return to square or near- square position before the close of business.

- It must be clearly understood that any temporary excesses over the approved daylight position limits will require approval of the bank management.
- In the smaller banks, it is the usual practice even to lay down a dealing limit for the dealer in each currency so that any deal individually larger than the approved limit will require prior approval of appropriate/ designated authority of the bank.

Overnight Limits

- The Exchange Control Rule requiring maintenance of square or near square position is adhered to as the exchange market conditions can be very fluid and unpredictable.
- Management keeps a close watch on the dealers' positions at the close of business each day - to ensure that the Exchange Control rule supplemented by the internal guidelines is observed.
- A statement of daily closing positions indicating the overbought and oversold positions, if any, held more than the daylight limits in the currency during the day (whatever be the time interval) and the limits (both daylight and overnight) laid down by the management should be submitted to the senior management official at the close of business daily.

The bank's top management should ensure that the dealers do not hold a position which can be considered as not being near square.

Any violations of the Exchange Control regulations in this regard are viewed adversely by the Reserve Bank.

Non-reporting days should be effectively curbed through the daily statements submitted to the authorities, supplemented by interval spot checks, wherever necessary.

Inter-Bank Limits

- Authorized dealers should set up limits for dealing with individual banks both in overseas banks as well as authorized dealers in India.

- While setting up limits, the capital plus reserves position of the other Bank, the manner of past dealings with the Bank and the market reports about the functioning of the Bank must be borne in mind.
- It is a common practice to lay down limits as a multiple of the last known capital plus the reserves position of the bank.
- In some cases, Balance sheet totals and assets coverage ratios may also be considered while limits are fixed or reviewed. Whatever be the procedure followed, dealings should be undertaken based on value of contracts concluded already and outstanding with the Bank so that the outstanding always are within set limits, any temporary excess being permitted with prior consent of the management.
- For this purpose, sales and purchases must be aggregated and not set off.
- All transactions, including TOM delivery and SPOT delivery contracts (but not ready or cash) should be reckoned for the purpose of monitoring inter-Bank limits.
- Extra care must be exercised if forward maturities get clustered around date(s) (months) and the credit risks on the relative settlement dates may be considered.
- While banks are free to set limits for the counterpart banks, according to the norms spelled out above they should not fix low limits (including refusal to deal) against banks on extraneous considerations such as deposit-grabbing or competition in exchange business.

Customer Limits

- Under the present Exchange Control regulations, all customer contracts for spot deliveries are deliverable on the same day.
- Further, customer forward contracts are permissible only if they are self-liquidating in nature, i.e., they are fulfilled by delivery of foreign exchange obligations arising from imports of goods or services.
- Speculative and trading contracts are prohibited.
- Even then, authorized dealers would do well to set limits for forward contracts for their larger customers so that the credit risks arising from such exposure can be periodically monitored.

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- Such limits may be laid down by the management wherever found appropriate and the monitoring conducted through the accounting department should maintain proper records of customer-wise outstanding liabilities under forward contracts.
- The transactions of fresh contracts and deliveries there against, handled for such customers, by the Foreign Exchange Department or by the branches should be required to be reported to the Accounting Department to enable it to perform the monitoring function effectively.

Organization of the Dealing Department

General

- Foreign exchange dealing is a highly specialized function and must be performed by a set of well-trained personnel.
- Typically, a Dealing Department should consist of dealers and backup staff who are responsible for the follow-up of the deals made by the dealers, giving feedback of collated information to the dealers, helping dealers to get overseas telexes and SWIFTS, checking rates, etc.
- There is a considerable scope of abuse by over-lapping of functions through manipulation of rates on contracts already concluded manipulation through position, mismatching, etc.
- The effectiveness of control over the dealing room largely depends on how the department is organized.
- With improvement in communication system, at present, in most of the Banks the Dealing Room is centralized.

Segregation of Dealing and Accounting Functions

- The dealing function must be separated from the accounting, funding and other backup functions.
- In the smaller banks, the functions should be assigned to different officers of the same rank reporting to a senior officer of the bank, so that the dealing and the backup functions are carried out by two or more persons, mutually supporting and drawing support and each acting as a check on the other in the larger interests of the Bank.
- The practice observed in certain banks whereby officers in senior ranks handle inter-Bank deals and control the funding and other backup functions.

Infrastructure of the Dealing Department

- For the Dealing Department to function effectively, it is necessary that the Managements in the banks provide adequate infrastructure to the Department.
- Independent telex/SWIFT machines (which can be kept locked by the Dealing Department), which contribute to efficient functioning of the Department, will protect banks from the activities of unauthorized persons with an intention of fraudulent foreign exchange deals on behalf of banks.
- Economic journals, newspapers, exchange market reports, reports from leading correspondent banks, money reports from organizations like Reuters video screen, etc., will greatly enhance the efficiency of the dealers.
- The larger banks generally provide separate rooms for dealing personnel with proper sound proofing, air-conditioning, stringent access control.

Duties of Dealers

- The duty of the dealers is to operate in the inter-bank market according to the guidelines laid down by the management of the bank from time to time.
- In the best interests of the bank, it is important to provide an effective and quick feedback to the management.
- The ideal arrangement will be for the dealers to confer before the work starts on the trend in the overnight markets and the markets still operating in the same time zone in the light of the overnight 'news bag' and the Bank's own business and arrive at tentative conclusions valid for the day.
- The dealer (or the Chief dealer) should keep the management informed of the conclusions.
- It is essential that the management should keep communication channels with dealers always open (by intercom, direct access, etc.) so that quick consultations are facilitated.
- In banks operating at various centres under a decentralized set up, the

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dealers operating at centres away from the Head Office should likewise constantly maintain contact with the local management responsible for the dealer's functions.

- The dealers could also communicate with the dealer (or the Chief dealer) at the Head Office to coordinate the market view.

Dealing Procedure

- The dealers should have no accounting work of any kind to perform, as they should always concentrate on the market through telex, telephones, video screen services, by maintaining contact with other banks, brokers as well as banks abroad.
- Deals made by the dealers should be recorded on printed 'Deal Slips'.
- The deal slips should indicate the name of the broker (if any), name of the counterparty Bank, currency, amount, rate and delivery, under the authentication of the dealer.
- Duplicate deal slips should be prepared preferably indifferent colours to identify sales and purchases.
- One copy will be retained with the Chief dealer/ Manager and the other, sent to the back-up staff for accounting and issue of contracts etc.
- Time at which the deal is put through should be invariably indicated in the deal slip.
- The deal slips should be passed on to the Accounting Department for further processing.

Dealers of Customers Business

- Large banks may find it advisable to deal selectively with customer enquiries regarding rates and conclude business with them in the Dealing Department, instead of in the Foreign Exchange Department.
- In such a setup, the dealers attending to customer business should, as far as possible, be distinct from the dealers in inter-Bank in order that the former may have the orientation required for customer dealing which is different from the one required for inter- Bank dealing.
- Such separation will also be in the interest of the Bank as possibilities of over familiarity between dealers in the Bank and customers exist.

Rotation of Dealers

- Dealers should not be kept for too long on dealing duties.
- A period of three to five years being considered as a reasonable period for effecting a change, training and substitution of dealers should be an on-going process so that the same personnel do not remain on dealing duties beyond a reasonable period in the interest of both the individual and the Bank.

Duties of Accounting Department

- For deals done through brokers, the Accounting Department should procure a receipt of exchange broker's notes irrespective of whether the deals have been done through brokers or directly.
- It is essential for the Accounting Department to confirm deals made by dealers by sending the requisite confirmation of contracts to the counterparty banks.
- Likewise, the accounting departments should monitor receipt of confirmation of contracts from counterparty banks and check the correctness thereof, by comparison with Deal Slips or the Bank wise record of inter-bank contracts maintained in the department.
- Confirmation of contracts must be obtained from the counterparty banks in each case.
- The signature of the official (who should be one other than the dealer) of the counterparty bank should be verified.
- An official of the Accounting Department authorized in this regard should likewise confirm contracts sent by counterparty banks under his signature.
- In no case should the dealer sign the contracts booked by them.
- Contracts, together with confirmations of counterparty banks should be systematically paired off and after verification inter-send with relative exchange broker's notes (in case of deals made through their medium), filed away in the accounting department for the purpose of record.
- Discrepancies should be brought to the notice of the dealers and should be rectified on the same day.
- Dealers in the dealing department maintain position pads and funds chart along with the statement of maturity pattern of the contracts.

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- These should be filed in seriatim and kept with the Dealing department for any future reference.
- They should also keep a track of the 'Nostro' balances based on cable advice received from overseas correspondents.
- Currency wise positions and funds positions should be communicated at frequent intervals to dealers who would be operating only based on deal slips sent by dealers and the reports of foreign exchange business flowing in from the Foreign Exchange Department and from other reporting branches.
- On grounds of convenience, the Accounting Department should be situated near the dealers.
- Apart from the position and Funds Records, the Accounting Department maintains all other records to facilitate submission of feedback and control information to dealers on the one hand and the Management of the Bank, on the other.
- The Accounting Department prepares bank-wise summaries of all outstanding forward exchange contracts with banks for which confirmations from counterparty bank have not been received as on the last working day of each month and have the outstanding confirmed by the counterpart banks.

Government Business by Agency Banks

Concurrent Auditor shall verify whether various types of government business like GST and Income Tax collection, PPF deposit and withdrawal, senior citizen saving scheme, etc are conducted as per the extant guidelines and circulars of the government and RBI.

Customer Service

- To check whether folder containing copies of both the codes / Customer Centric Policies / Interest rates / Charges / Banking Ombudsman Scheme is available with the branch manager (The information should be latest and updated in the folder).
- To check whether the Cheque drop box is available at branch & it is being opened daily, and the cheques are taken out.

- To check whether the suggestion box is available at branch, suggestion box/ register is available in ATM Cabin and whether suggestion box is being opened fortnightly/ register is being checked fortnightly.
- To check whether the Banking Ombudsman Scheme and the details of the Ombudsman for the region are displayed on the branch notice boards.
- To check whether time norm boards are displayed at the branch.
- To check whether the latest interest rates on deposits & loans and the charges schedule is displayed on the notice board.
- To check whether complaint redressal hierarchy with names and phone numbers is displayed in the branch.
- To check whether it is displayed that 'Nomination facility is available here for all deposit accounts.
- To check whether 'The BCSBI membership certificate' and the fact that 'the folder & the codes are available with the branch manager' is displayed at the branch notice board.
- To check whether notice about 'the BSBDA small accounts with concessional KYC are opened in the branch' is displayed.
- To check whether the notice that the forged note detected by the cashier will not be returned to the customer and it will be impounded is displayed at the cashier counter. To check the acknowledgements given to the customer for impounding the notes (if any) are maintained on record.
- To check whether the posters prescribed by RBI for detection of forged notes are displayed at branches.
- To check whether the minutes of the Branch Customer Service Committee meetings are kept on record.
- To check whether the periodical record of complaints received is kept and sent to the AGM for forward reporting.
- To check whether the minutes of the Branch Customer Service Committee meetings are kept on record.

Branch Security Aspects

- Concurrent Auditor should verify whether adequate security is provided at the branch by way of security guard as per policy of the bank.
- The concurrent auditor should also verify whether CCTV cameras are working effectively and should ensure that regular backups are taken and maintained.
- The concurrent auditor should also see that adequate fire extinguishers are in place and replaced at periodic intervals.

Chapter 3

Conduct of Concurrent Audit

- 3.1 Concurrent audit is to be conducted according to the guidelines and instructions given by the bank in that regard. However, the basic needs of the Concurrent audits are generally the same in all the banks.

3.2 Appointment Letter and Expectations of the Bank

- i. Individual Banks periodically carry out process of empanelment of Concurrent Auditors, based on various criteria determined by them. Chartered Accountants are required to furnish various details regarding the firm, bank audit experience etc. After empanelment and selection of the auditor, letter of appointment will be sent to the Auditor communicating the branches to be audited. Necessary instructions / guidelines for conducting the audit, scope of the audit assignment, minimum areas to be covered, frequency of conducting the audit etc. will also be communicated along with the letter of appointment.
- ii. After receipt of letter of appointment, Auditor is required to communicate acceptance of the assignment, in the format prescribed by the bank, if any, along with declaration of confidentiality and secrecy, Non-disclosure Agreement, and various other undertakings, as prescribed by the bank.
- iii. The Concurrent Auditor should also send "Letter of Engagement" as prescribed by the ICAI, confirming the understanding of mutual responsibilities upon which the auditor is engaged to perform various professional services for the bank.
- iv. The appointed concurrent auditor should communicate to previous concurrent auditor informing him the appointment and requesting him to inform any objection for such appointment, if any.
 - (a) This appointment is the agreement between Bank and auditor describing terms of contract, scope of audit and other related terms of reference, such as, time allotted, frequency of checking, etc.
 - (b) The concurrent auditor should mention the reference of this

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appointment letter in audit programme and letter covering the report.

The concurrent auditor would, therefore, need to have the following documents before the commencement of the audit:

- The appointment letter together with the management circular/ instructions on the subject.
- Acceptance Letter.
- Communication to previous auditor.

A checklist or flow till commencement of Concurrent Audit of the branch is given below:

- A. On receipt of appointment letter:
- Write a Letter to the immediate previous auditor to communicate your appointment & seeking their objections, if any:
 - Send Acceptance letter in the Letter Head of the Chartered accountant along with statement of Declaration of Fidelity and Secrecy, Confidentiality, etc.
 - Contact the respective Branch Manager – for programme, arrangement and status report.
 - Prepare the Concurrent Audit Programme.
- B. To carry with branch during their visit to the branch:
- Authorization Letter.
 - Necessary guidelines.
 - Various Formats.
 - Letter head of the Concurrent Auditors / Audit Firm.
 - Digital Key of Chartered Accountant.
 - Rubber Stamp (seal) of the Audit Firm.

General Reference

For the purpose of concurrent audit, the general references should be drawn from the sources, including:

Conduct of Concurrent Audit

- Bank's Book of Instructions.
- Bank's Manual on Documentation.
- Master Circulars, Master Directions and other circulars / notifications issued by the Reserve Bank of India from time to time. (<https://www.rbi.org.in/Scripts/NotificationUser.aspx>)
- Exchange Control Manual and Rules of FEDAI (Foreign Exchange Dealers Association of India).
- Internal Inspection Report & Risk Based Internal Inspection / Audit Report of the Branch.
- Long Form Audit Report (LFAR) of the statutory auditor.
- Visit Reports of Executives from controlling offices (ZO/HO).

ICAI References-

- Guidance Note on Audit of Banks (this is revised every year & latest edition be referred).
- Technical Guide on Audit of Internal Financial Controls in case of Public Sector Banks.
- Technical guide on Stock & Receivables Audit.
- Early Signals of Fraud in Banking Sector.
- Compliance with Standards on Internal Audit Standards

Concurrent Auditor should ensure compliance of various Standards on Internal Audit (SIA) issued by the ICAI by visiting <https://internalaudit.icai.org/standards-on-internal-audit/>.

Commencement of Concurrent Audit

Understanding the Bank and the Branch

If the Concurrent Auditor is conducting audit of the particular bank for the first time, he should understand following aspects about the Bank and the Branch:

About the Bank

- Management Structure of the Bank (Head Office, Zonal / Regional

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Offices, branches)

- Various departments at the Head Office / Zonal / Regional Office of the Bank to which the Branch is reporting
- Centralisation / De-centralisation of various functions, like processing of loan applications, KYC formalities of customers, interest application etc.
- Core Banking Software and other important softwares used at the Branch (Auditor can request for specific training / walkthrough of the software, so as to facilitate conducting concurrent audit. This is essential if auditor is conducting audit under that software for the first time)
- Various reports available from CBS, which are essential for conducting the concurrent audit
- Various products under deposits and loans portfolios of the Bank, their features, policies, rules and regulations thereof
- Areas to be covered under Concurrent Audit & frequency thereof (Daily, weekly, fortnightly, monthly, quarterly, half yearly, annual basis as per the details given along with appointment letter)
- Web-based / Application software used for the purpose of preparation of concurrent audit report, its' features and requirements

About the Branch

- Type & Size of the Branch (Metropolitan, Urban, Semi-urban, Rural) & Very Large Branch (VLB) Exceptionally Large Branch (ELB) Corporate / Industrial Finance Branch, Agricultural, SME, Retail, etc.
- Various loan and deposit products handled by the Branch, other banking services given by the Branch such as safe deposit lockers, ATM,
- Various departments / sections in the branch and officials-in-charge
- Review of Trial balance of the Branch on a latest date
- Understanding loan & deposit portfolio of the Branch in order to focus the audit plan & verification, team size and composition etc.

Review of Past Reports

The concurrent auditor would also need to go through the previous reports of the Branch such as:

1. The statutory audit reports and Long Form Audit Reports (LFAR)
2. Internal inspection reports and Risk Based Inspection / Audit Report.
3. RBI inspection reports.
4. Stock audit report.
5. Earlier year's Concurrent audit reports of the branch.

Apart from the above the Concurrent auditor should call for the following reports, which will be useful in conducting the Concurrent Audit:

- Credit Audit Report.
- Revenue Audit Report.
- System Audit Report.
- NPA Audit Report.
- Gold Loan Verification Report.
- Housing Loan Verification Report.
- Legal Audit Report
- Subsidy Verification Report, etc.

Review of these past reports will be useful for the Concurrent Auditor to understand areas of strengths and weaknesses in the branch and accordingly thrust to be given while conducting concurrent audit.

Arrangement of Infrastructure

Concurrent Auditor in consultation with the branch authorities shall organise for following infrastructure to facilitate smooth conduct of audit:

- Proper sitting arrangement for the members of the audit team
- Computer terminals with access to CBS and any other application software of the Bank, to be used for conducting concurrent audit
- Access to various types of reports such as daily reports, monthly

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reports, exceptional reports, etc.

- Communication facilities including email

Business Profile of the Branch

Business Profile is essential before initiating Concurrent Audit of the branch.
A model of profile is given below:

Business Profile of Branch

- (i) Name of the Branch :
- (ii) Date of Opening of Branch :
- (iii) Area Classification – Metro/Urban/Semi-Urban/Rural :
- (iv) Category of Branch – Exceptionally Large/Very Large/Medium/Small :
- (v) Risk – High/Medium/Low :
- (vi) Whether Branch is provided with :
 - (a) Currency Chest : Yes/No
 - (b) Safe Document Vault : Yes/No
 - (c) Safe Deposit Locker : Yes/No
 - (d) ATM Facility : Yes/No
- (vii) Whether Branch carries out/ has the facility of:
 - (a) Foreign Exchange Business : Yes/No
 - (b) Govt. Business : Yes/No
 - (c) Merchant Banking Business : Yes/No
 - (d) Mechanisation with CBS (Core Banking System) : Yes/No
- (viii) Particulars of the Manager-in-charge of the Branch :

Tenure in the Branch			
Name	Scale	from	To
Existing			

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Previous

(ix) Date of last internal inspection: Date of submission of Rectification Confirmation

Date of closure of Report:

Date of last concurrent audit:

Date of submission of Compliance Report/ Rectification Confirmation

Date of closure of Report

BUSINESS OF THE BRANCH

Name of the Branch.....

For the Month/Quarter ended.....

(a) Synopsis of Assets & Liabilities

`/Lacs

	Position		
Assets	As on the last day of the financial year	As of last day/ Friday of the previous month/ quarter	As of last day/ Friday of current month/ quarter
Cash			
Balance with Banks			
Investments			
Advances			
Inter Branch Transaction (Net Dr)			
Other Assets			
P/L/ A/c (Dr. Balance)			
Contra Liabilities			
Contra Liability for Instruments on			

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collection basis			
Total			
Liabilities			
Deposits			
Borrowing from Banks			
Inter Branch Transaction			
Other Liabilities			
P/L/ A/c			
Contra Liabilities			
Contra Liability for instruments on collection basis			
Total			

(b) Business Parameters

Particulars	Position	
	As of last day of the previous month/ quarter	As of last day of current month/ quarter
Deposits of which low-cost deposits		
Deposits at non-card rates		
Advances		
Non-performing Assets (NPA) % to total advances and Fresh NPAs/ Recovery performance. <ul style="list-style-type: none"> • of which cash recovery • Other than cash recovery • Priority sector advances Export Credit • Fresh NPAs 		

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Profit Staff Productivity Observations on sudden spurt or fall in Deposits and Advances.		
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Audit Planning

As part of Planning Concurrent Auditor is expected to study and understand various legal and regulatory provisions. It is suggested that Concurrent Auditor shall download all the latest Master Directions, Master Circulars and Relevant Notifications issued by RBI from time to time. Compliance of these legal and regulatory provisions shall be considered while planning the concurrent audit.

Access to various Standard Operating Procedures and Circulars issued by the particular Bank under audit shall also be given to the Concurrent Auditor. The same should be studied thoroughly in order to ensure compliance of the same by the Branch under audit.

The Bank will provide broad / detailed scope of the Concurrent Audit and also the frequency of the activities i.e. activities to be carried out on daily, weekly, fortnightly, monthly basis and also quarterly, half yearly and annual basis.

Based on both these documents and also nature and size of products & services handled and business activities carried out by the Branch, the Concurrent Auditor should prepare detailed audit plan consisting of areas to be covered, their frequency team member allocated to the area etc. The plan should be discussed and thoroughly explained to the audit team members, so as to facilitate their execution by the team.

Details of actual work carried out should also be incorporated against the plan, which will form working paper of audit execution for the month. This will help the Concurrent Auditor for review of actual work carried out against the plan and taking steps for deviations, if any. Such month-wise files should be retained for future reference.

- (a) After completion of each Monthly/Quarterly audit, the Progress Report should be updated to enable the subsequent concurrent auditor to take up the audit for subsequent months.

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- (b) From the follow-up sheet (indicating what areas are due to be completed), the routine as well as the 'important' areas may be decided during the month and reported under appropriate head of accounts.
- (c) After completion of drafting of the monthly report, again a 'Follow up' sheet should be prepared for the next month. This process should be continued till the last month of the concurrent audit period.
- (d) This will ensure that all the areas of the Bank's functioning have been covered by the audit team during the 'concurrent audit year'.
- (e) In absence of any specific guidelines by the Bank, all credit facilities/ arrangements should be audited at least once during one concurrent audit year.
- (f) The concurrent auditor should not confine their areas of functioning to instructions on subject matter already given to them in writing but should also use their own judgment and wisdom to cover such other matters which might lead to a financial loss subsequently.

Preparation of Audit Programme

Following points are required to be kept in mind by concurrent auditor while preparing audit program:

- (i) The Concurrent Auditor shall ensure the compliance of Standards on Internal Audit issued by Internal Audit Standard Board of ICAI.
- (ii) The concurrent auditor should prepare a formal concurrent audit programme listing the procedures essential for meeting the objective of the concurrent audit plan.

This audit programme should be prepared in such a manner to cover the entire audit areas as specified under the scope of concurrent audit and easily modifiable to the needs of the Bank audit.

- (iii) This audit programme should be discussed with the entire audit team of the Concurrent auditor and explained to the audit staff. The audit staff must understand the techniques and issues of audit programme in advance, so that the Concurrent audit will be carried out in a successful manner.
- (iv) Though the form and content of the audit programme and the extent of its details would vary with the circumstances of each

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case, yet the concurrent audit programme should be so designed as to achieve the objectives of the engagement and also provide assurance that the concurrent audit is carried out in accordance with the Standards on Internal Audit issued by Institute of Chartered Accountants of India.

- (v) The concurrent audit programme identifies, in appropriate details, the objectives of the concurrent audit in respect of each area, the procedures to be performed to achieve those objectives, the staff responsible for carrying out the activity, the time allocated to each activity as also the sufficiently detailed instruction to the staff as to how to carry out those procedures.
- (i) The concurrent audit programme may also have provision for information, such as, the procedures performed, reasons for not performing the originally identified procedures, actual time consumed in carrying out the relevant procedure, reasons for deviations from budgeted time, etc.
- (ii) A well-prepared, comprehensive audit programme helps proper execution of the work as well as of the proper supervision, direction and control of the performance of the engagement team.

Documentation & Working Papers

The concurrent auditor should document matters which are important in providing evidence that the concurrent audit was carried out in accordance with the basic principles of an audit and as per terms of reference. The Institute has also issued Standard on Internal Audit (SIA) 330, *Internal Audit Documentation*. This should also be referred for the purpose.

The concurrent auditor should record the audit plan as per the checklist and the format of audit report given by the respective bank's circulars, terms of engagement, scope of work, etc., and the engagement letter should also be taken into consideration in this regard.

The Concurrent Auditor may keep in mind following points while documenting working papers:

- (i) The concurrent auditor should keep all the working papers on

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record which are prepared during conduct of audit and used in finalizing the reports. The working papers shall be maintained in hard / print form, wherever possible and entire set in electronic form (in combination of MS Excel and MS Word)

- (ii) Keeping working papers will help the Concurrent auditor from lot of technical issues and facing the Code of Ethics, if any.

Permanent Audit File

The following papers can be kept in permanent audit file:

- Letter of engagement, undertaking by the firm to the bank.
- Detailed list of all the decisions taken with Notes on record.
- Audit checklist.
- Information regarding branch business, data, nodal officer, status of branch, whether computerized/parallel category of branch, etc.
- Correspondence with the bank for any matter.

Current Audit File

Similarly, the current audit file may include audit working papers and all other papers relevant to the concurrent audit, for example:

- (i) Branch Audit Programme.
- (ii) Branch's statement / trial balance as on the date of the report on which basis it is prepared.
- (iii) Periodic correspondence with the concerned departmental officers.
- (iv) Irregularities intimated to the Controlling Officer.
- (v) Discussion of the audit report.
- (vi) Particulars of big borrowers, depositors, etc.
- (vii) Circulars received from head office of the audited bank.
- (viii) Audit checklist with details of audit work carried out for the particular month.
- (ix) Queries sent to the branch officials and replies / responses

received thereon, compliance status and reference to the audit report.

Working papers in current audit file may be maintained in electronic form by properly grouping them in the folder with appropriate file names for various files in electronic form.

It is necessary for the auditor to record his observations in an appropriate record and bring them to the notice of concerned official of the Bank.

An auditor's observations should be reported immediately if the observation is very important and requires immediate rectification. The report should be made to the "Reporting authority" as mentioned in the Appointment letter.

Frequency of Checking Different Items

- (i) The frequency of checking of different items by the concurrent auditor depends on factors, such as, the guidelines given by the bank in the scope of work, size & nature of the business at the Branch etc.
- (ii) A concurrent auditor needs to devise his own strategy/timeframe covering all the areas.
- (iii) For this purpose, the auditor would need to first identify the areas at the branch which need greater attention, the areas which are to be regularly monitored, the items which are to be checked daily, and the items which may be checked less frequently.
- (iv) This frequency of checking of different items should be included in the Concurrent Audit Programme, which should be based on the instructions given at the Appointment Letter issued by the Bank's Head office.
- (v) Certain exceptional transactions reports / control reports will have to be verified on daily basis, as specified in the terms of reference. The Auditor should ensure that these reports are critically examined by him and persistent irregularities, if any, are brought to the notice of bank's management at appropriate level (branch / controlling office / head office) for corrective actions and to ensure that such irregularities are not repeated.

Maintenance of Appropriate Records

Concurrent auditor shall maintain record of discrepancies / irregularities / observations and communicate the same to the concerned departments / officials of the Branch, to the Nodal Officer / Branch Manager. Such record can be maintained in electronic form (such as in MS Excel), in suitable format devised for this purpose and can be communicated to the Branch by email, either on daily basis or after completion of audit of the particular area.

Various items to be, normally, recorded are given below:

Area	Account No. / Transaction Ref. No.	Date of Transaction	Name of the Borrower / Customer	Amount Rs.

Irregularity Observed	How Irregularity Was Rectified	Date of Rectification	Reference to the Audit Report
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Separate sheets may be used department-wise / discrepancy-wise such as for Deposits Section - Savings A/c Opening Forms, Current A/c Opening Forms etc. Advances Section (Vehicle Loans, Personal Loans etc.)

The recording should be made daily with date with suitable column for recording rectification/removal.

The record should be made available to the officer in charge of the controlling office or their representatives as and when they visit the branch to apprise them of the state of working of the branch, removal/rectification of irregularities by the branch, compliance of systems and procedures by the branch.

Reporting System

- (i) Banks have devised concurrent audit reporting system in web-based

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application software and the audit reports are required to be prepared and submitted in that format only. The Concurrent Auditor should get acquainted with the features and requirements of the audit report software used by the bank under the audit. He should plan the audit and arrange details noted during the course of audit, in such a way that various parts & annexures in the web-based audit report can be properly and easily filled up without loss of time.

Periodicity of various check list items as per its sensitivity shall be given in the letter of appointment of the auditor. The auditor may decide the frequency for items not covered therein, if any.

- (ii) Minor irregularities pointed out by the concurrent auditors are to be rectified on the spot.
- (iii) Serious irregularities should be straightaway reported to the Controlling Offices/Head Offices for immediate action.
- (iv) The concurrent auditor would have asked some details/ records to be produced by the Banker, and the banker has refused to produce / not produce the same for some other reasons. These facts must also be included in the Reporting system by the Branch Concurrent Auditor.
- (v) Whenever fraudulent transactions are detected, they should immediately be reported to Inspection and Audit Department (Head Office) as also to the Chief Vigilance Officer as well as Branch Managers concerned (unless the branch manager is involved).
- (vi) Sometimes as per the Appointment letter, those detected fraudulent transactions have to be reported to RBI and the Concurrent auditor has to report the same to RBI. But it is advised that the Concurrent auditor must have the base records and evidence on his record before reporting the Fraudulent Transaction to Bank as well as RBI.
- (vii) It is to be noted that the Concurrent Auditor has to report the Fraudulent transactions only to those persons' names mentioned in the Appointment letter / RBI Guidelines / Banks' Circulars. In any situation the details of Fraudulent Transactions should not be revealed to anyone, otherwise the Concurrent auditor is held responsible by Bankers, as he has signed "Declaration of Fidelity and Secrecy" at the time of acceptance of audit.
- (viii) A special report may be submitted by the concurrent auditor in

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situations of any serious irregularity/ frauds, etc. In such cases, the concurrent auditor should get in touch with the higher authorities at the earliest besides sending a special report/flash report to the higher authorities, explaining the findings of the case.

- (ix) The issue needs to be discussed with the Branch manager and his feedback/ views to be mentioned in his special report:
 - (a) There should be proper reporting of the findings of the concurrent auditors. For this purpose, each bank should prepare a structured format.
 - (b) The major deficiencies/aberrations noticed during concurrent audit should be highlighted in a special note and given immediately to the bank's branch controlling offices.

Rectification of Irregularities

- (i) To supplement the process of removal/rectification of irregularities in the earliest possible period, the concurrent auditor will bring his finding of the irregularities/ deficiencies/discrepancies to the notice of the branch officials.
- (ii) The outstanding deficiencies/irregularities need to be discussed with branch officials and their viewpoints also need to be reflected.
- (iii) The concurrent auditor should maintain an appropriate record of the irregularities observed as well as the discussions held with the branch officials.
- (iv) Pending irregularities not rectified would be included in the final report of the concurrent auditor.
- (v) Concurrent Auditor should not leave any irregularities, whether it is material or not, and cover the same in his report.
- (vi) Even the Rectified irregularities should also be covered in his report as:
 - The irregularity of transactions pointed out (list the same) by the Concurrent auditor have been rectified by the Branch and the view of Concurrent auditor should also be recorded.
- (vii) Materiality of the irregularities should be clearly spelt out in the final report.

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- (viii) The irregularities pointed out in the previous monthly/quarterly concurrent audit reports may be dropped by the concurrent auditor with proper disclosure if the same have been rectified.
- (ix) In case the branch officials do not co-operate in rectification of the irregularities, the concurrent auditor may contact/ write to the higher authorities. It is better to avoid “oral” discussion in this matter.

Chapter 4

Prudential Norms for Assets Classification, Income Recognition and Provisioning Pertaining to Advance

Introduction

- 4.1 Every year, RBI consolidates instructions/ guidelines issued on matters relating to prudential norms on income recognition, asset classification and provisioning pertaining to advances. RBI Master Circular No. RBI/2025-26/13 DOR.STR.REC.9/21.04.048/2025-26 dated April 1, 2025 “Master Circular – Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances” incorporates and updates instructions issued up to 31.03.2025.
- 4.2 The policy of income recognition should be objective and based on record of recovery rather than on any other subjective considerations. Likewise, the classification of assets of banks must be based on of objective criteria which would ensure a uniform and consistent application of the norms.
- 4.3 The provisioning should be made based on the classification of assets based on the period for which the asset has remained non-performing and the availability of security and the realizable value thereof.
- 4.4 As per the above-mentioned RBI Circular, banks are urged to ensure that while granting loans and advances, realistic repayment schedules may be fixed based on cash flows with borrowers. This would go a long way to facilitate prompt repayment by the borrowers and thus, improve the record of recovery in advances.

Non-performing Assets

- 4.5 An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. A non-performing asset (NPA) is a loan or an advance where:
 - (a) Interest and/ or instalment of principal remain overdue for a period of more than 90 days in respect of a term loan.

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- (b) Overdraft/Cash Credit (OD/CC) accounts remain 'out of order' when, outstanding balance remains continuously more than the sanctioned limit/ drawing power for 90 days. In cases where outstanding balance in the principal operating account is less than the sanctioned limit/drawing power, but there are no credits continuously for 90 days, or credits are not enough to cover the interest debited during the same period (i.e., 90 days).
 - (c) The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.
 - (d) In respect of agricultural loan, the instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops.
 - (e) The instalment of principal or interest thereon remains overdue for one crop season for long duration crops.
 - (f) The amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitization transaction undertaken in terms of the Reserve Bank of India (Securitisations of Standard Assets) Directions, 2021.
 - (g) In respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.
- 4.6 In case of interest payments, banks should classify an account as NPA only if the interest debited and due is not serviced over 90 days when it became due. In addition, an account may also be classified as NPA in terms of following paragraph:

Accounts with Temporary Deficiencies

- 4.7 The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as:
- (a) Non-availability of adequate drawing power based on the latest available stock statement.
 - (b) Balance outstanding exceeding the limit temporarily.

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- (c) Non-submission of stock statements.
- (d) Non-renewal of the limits on the due date, etc.

In the matter of classification of accounts with such deficiency's banks may follow the following guidelines:

- (a) Banks should ensure that drawings in the working capital accounts are covered by the adequacy of current assets, since current assets are first appropriated in times of distress. Drawing power is required to be arrived at based on the stock statement which is current. However, considering the difficulties of large borrowers, stock statements relied upon by the banks for determining drawing power should not be older than three months. The outstanding in the account based on drawing power calculated from stock statements older than three months, would be deemed as irregular and will be NPA at the end of 180 days.
- (i) Where the stock statement is required to submit monthly; The OCC account become NPA at the end of 90 days from the end of the month in which stock statements not submitted.
- (ii) Where the stock statement is required to submit quarterly; The OCC account become NPA at the end of 180 days from the end of the month in which stock statements not submitted.

A working capital borrower account will become NPA if such irregular drawings are permitted in the account for a continuous period of 90 days even though the unit may be working well, or the borrower's financial position is satisfactory. For instance, an OCC account was not operated within the limit or DP during any one occasion of 90 days, that account needs to be classified as NPA on 90 days of such continuous over drawings.

- (b) Regular and adhoc credit limits need to be reviewed/ regularized not later than three months from the due date/date of ad hoc sanction. In case of constraints such as non-availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal/ review of credit limits is already on and would be completed soon. In any case, delay beyond six months from the date of due for renewal is not considered desirable as a general discipline. Hence, an account where the regular/ ad hoc credit limits have not been reviewed/ renewed within 180 days from the due date/ date of adhoc sanction will be treated as NPA. It may further be noted that only

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the date of Regular Review should be considered for this purpose and Short or ad-hoc reviews done for a temporary period of 90 days should not be considered.

Asset Classification

4.8. Broadly, advances are categorized into following four heads:

- Standard Assets
- Sub-Standard Assets
- Doubtful Assets
- Loss Assets

Standard Assets

A Standard Asset is one which does not disclose any problem, and which does not carry more than normal risk attached to the business. Such an asset is not a non-performing asset.

Sub-standard Assets

With effect from March 31, 2005, a substandard asset would be one, which has remained NPA for a period less than or equal to 12 months. Such an asset will have well defined credit weaknesses that jeopardize the liquidation of the debt and are characterized by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.

Doubtful Assets

With effect from March 31, 2005, an asset would be classified as doubtful if it has remained in the substandard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, – based on currently known facts, conditions and values – highly questionable and improbable.

Loss Assets

A loss asset is one where loss has been identified by the bank; or internal or external auditors; or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable

asset is not warranted although there may be some salvage or recovery value.

Upgradation of loan accounts classified as NPAs

- 4.9 The loan accounts classified as NPAs may be upgraded as 'standard' asset only if entire arrears of interest and principal are paid by the borrower. In case of borrowers having more than one credit facility from a bank, loan accounts shall be upgraded from NPA to standard asset category only upon repayment of entire arrears of interest and principal pertaining to all the credit facilities. Regarding upgradation of accounts classified as NPA due to restructuring, non-achievement of date of commencement of commercial operations (DCCO), etc., the instructions as specified for such cases shall continue to be applicable.

Income Recognition Policy

- 4.10 The policy of income recognition must be objective and based on the record of recovery. Internationally income from non-performing assets (NPA) is not recognized on accrual basis but is booked as income only when it is received. Therefore, the banks should not charge and take to income account interest on any NPA. This will apply to Government guaranteed accounts also.

However, interest on advances against Term Deposits, National Savings Certificates (NSCs), Indira Vikas Patras (IVPs), Kisan Vikas Patras (KVPs) and Life Insurance policies may be taken to income account on the due date, provided adequate margin is available in the accounts.

Fees and commissions earned by the banks because of renegotiations or rescheduling of outstanding debts should be recognized on an accrual basis over the period covered by the renegotiated or rescheduled extension of credit.

In cases of loans where moratorium has been granted for repayment of interest, income may be recognised on accrual basis for accounts which continue to be classified as 'standard'. This shall be evaluated against the definition of 'restructuring' provided in paragraph 16 of the RBI's Master Circular.

Income recognition norms for loans towards projects under implementation involving deferment of DCCO shall be subject to the instructions contained in paragraph 4.2.15 of the RBI's Master Circular

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and that for loans against gold ornaments and jewellery for non-agricultural purposes shall be subject to the instructions contained in circular DBOD.No.BP.BC.27/21.04.048/2014-15 dated July 22, 2014 on the subject, as updated from time to time.

Reversal of Income

- 4.11 If any advance, including bills purchased and discounted, becomes NPA, the entire interest accrued and credited to income account in the past periods should be reversed if the same is not realised. This will apply to Government guaranteed accounts also.

If loans with moratorium on payment of interest (permitted at the time of sanction of the loan) become NPA after the moratorium period is over, the capitalized interest, if any, corresponding to the interest accrued during such moratorium period need not be reversed.

In respect of NPAs, fees, commission and similar income that have accrued should cease to accrue in the current period and should be reversed with respect to past periods, if uncollected.

Leased Assets

The *finance charge* component of finance income [as defined in 'AS 19 Leases')] on the leased asset which has accrued and was credited to income account before the asset became non-performing, and remaining unrealised should be reversed or provided for in the current accounting period.

Appropriation of Recovery in NPAs

- 4.12 Interest realized on NPAs may be taken to income account provided the credits in the accounts towards interest are not out of fresh/ additional credit facilities sanctioned to the borrower concerned. In the absence of a clear agreement between the bank and the borrower for the purpose of appropriation of recoveries in NPAs (i.e., towards principal or interest due), banks should adopt an accounting principle and exercise the right of appropriation of recoveries in a uniform and consistent manner.

In the absence of a clear agreement between the bank and the borrower for the purpose of appropriation of recoveries in NPAs (i.e. towards principal or interest due), banks should adopt an accounting principle and exercise the right of appropriation of recoveries in a uniform and consistent manner.

Interest Application

- 4.13 On an account turning NPA, banks should reverse the interest already charged and not collected by debiting Profit and Loss account and stop further application of interest. However, banks may continue to record such accrued interest in a Memorandum account in their books. For computing Gross Advances, interest recorded in the Memorandum account should not be considered.

Provisioning Norms

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

In conformity with the prudential norms, provisions should be made on the non-performing assets based on classification of assets into prescribed categories. Considering the time lag between an account becoming doubtful of recovery, its recognition as such, the realization of the security and the erosion over time in the value of security charged to the bank, the banks should make provision against substandard assets, doubtful assets and loss assets as below:

Loss Assets

Loss assets should be written off. If loss assets are permitted to remain in the books for any reason, 100 percent of the outstanding should be provided for.

Doubtful Assets

100 percent of the extent to which the advance is not covered by the realizable value of the security to which the bank has a valid recourse, and the realizable value is estimated on a realistic basis. Auditor should verify whether that security is considered based on the latest information available with the bank.

Regarding the secured portion, provision may be made on the following basis, at the rates ranging from 25 percent to 100 percent of the secured portion depending upon the period for which the asset has remained doubtful:

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Period for which the advance has remained in doubtful category	Provision requirement (%)
Up to One Year	25
One to three years	40
More than three years	100

Valuation of Security

4.15 With a view to bringing down divergence arising out of difference in assessment of the value of security, in cases of NPAs with balance of Rs. 5 crore and above stock audit at annual intervals by external agencies appointed as per the guidelines approved by the Board would be mandatory to enhance the reliability on stock valuation. Primary securities as well as Collaterals such as immovable properties charged in favour of the bank should be got valued once in three years by valuer appointed as per the guidelines approved by the Board of Directors.

Sub-standard Assets

A general provision of 15 percent on total outstanding should be made without making any allowance for ECGC guarantee cover and securities available.

The 'unsecured exposures' which are identified as 'substandard' would attract additional provision of 10 per cent, i.e., a total of 25 per cent on the outstanding balance. However, in view of certain safeguards, such as, escrow accounts available in respect of infrastructure lending, infrastructure loan accounts which are classified as sub-standard will attract a provisioning of 20 per cent instead of the aforesaid prescription of 25 percent. To avail this benefit of lower provisioning, the banks should have in place an appropriate mechanism to escrow the cash flows and have a clear and legal first claim on these cash flows.

Provision on Standard Advances

Banks should make general provision for standard assets at the following rates for the funded outstanding on global loan portfolio basis:

- (a) Farm Credit to agricultural activities, individual housing loans and Small and Micro Enterprises (SMEs) sectors at 0.25 per cent.

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- (b) Advances to Commercial Real Estate (CRE) Sector at 1.00 per cent.
- (c) Advances to Commercial Real Estate – Residential Housing Sector (CRE - RH) at 0.75 per cent.
- (d) Housing loans extended at teaser rates prescribed up to 2% (subject to certain conditions).
- (e) Restructured advances – as stipulated in the prudential norms for restructuring of advances.
- (f) Advances restructured and classified as standard in terms of the Master Direction –Reserve Bank of India (Relief Measures by Banks in Areas affected by Natural Calamities) Directions 2018 – SCBs, as updated from time to time, at 5%.
- (g) All other loans and advances not included in (a) – (f) above at 0.40 percent.

Appropriate Internal Systems for Proper and Timely Identification of NPAs

- 4.16 Banks should establish appropriate internal systems (including technology enabled processes) for proper and timely identification of NPAs, including putting in place the necessary infrastructure to comply with the requirements of the circular DoS.CO.PPG./SEC.03/11.01.005/2020-21 dated September 14, 2020, on Automation of Income Recognition, Asset Classification and Provisioning processes in banks (as updated). To ensure the completeness and integrity of the automated Asset Classification (classification of advances/investments as NPA/NPI and their upgradation), Provisioning calculation and Income Recognition processes, banks are advised to put in place / upgrade their systems to conform to the following guidelines latest by June 30, 2021.

Other Important Issues

- 4.17 Some other important issues relating to IRAC has been given in brief in the following paragraphs. For further information, it is recommended to refer to the applicable Master Circular issued by the RBI every year.

Advances covered by ECGC guarantee:

In the case of advances classified as doubtful and guaranteed by ECGC, provision should be made only for the balance more than the

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amount guaranteed by the Corporation. Further, while arriving at the provision required to be made for doubtful assets, realisable value of the securities should first be deducted from the outstanding balance in respect of the amount guaranteed by the Corporation and then provision shall be made.

Exposures guaranteed by Credit Guarantee Schemes:

In terms of circular DOR.STR.REC.67/21.06.201/2022-23 dated September 07, 2022, banks have been permitted to apply zero risk weight to advances guaranteed by Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE), Credit Risk Guarantee Fund Trust for Low Income Housing (CRGFTLIH) and individual schemes under National Credit Guarantee Trustee Company Ltd (NCGTC), subject to certain conditions. In case such advances become nonperforming, no provision need be made towards the guaranteed portion. The amount outstanding, more than the guaranteed portion, should be provided for as per the extant guidelines on provisioning for non-performing assets.

Specification of due date/repayment date

- 4.18 The exact due dates for repayment of a loan, frequency of repayment, breakup between principal and interest, examples of SMA/NPA classification dates, etc. shall be clearly specified in the loan agreement and the borrower shall be apprised of the same at the time of loan sanction and also at the time of subsequent changes, if any, to the sanction terms/loan agreement till full repayment of the loan. In cases of loan facilities with moratorium on payment of principal and/or interest, the exact date of commencement of repayment shall also be specified in the loan agreements. These instructions shall be complied with at the earliest, but not later than December 31, 2021, in respect of fresh loans. In case of existing loans, however, compliance to these instructions shall necessarily be ensured as and when such loans become due for renewal/review.

Consumer Education

- 4.19 With a view to increasing awareness among the borrowers, banks shall place consumer education literature on their websites, explaining with examples, the concepts of date of overdue, SMA and NPA classification and upgradation, with specific reference to day-end process. Banks may also consider displaying such consumer education literature in

their branches by means of posters and/or other appropriate media. Further, it shall also be ensured that their front-line officers educate borrowers about all these concepts, with respect to loans availed by them, at the time of sanction/disbursal/renewal of loan.

Accounts Regularised near about the Balance Sheet Date

- 4.20. The asset classification of borrower accounts where a solitary or a few credits are recorded before the balance sheet date should be handled with care and without scope for subjectivity. Where the account indicates inherent weakness based on the data available, the account should be deemed as an NPA. In other genuine cases, bank must furnish satisfactory evidence to the auditors about the manner of regularisation of the account to eliminate doubts on their performing status.

Asset Classification to be Borrower-wise and not Facility-wise

- 4.21 If one facility provided to the borrower becomes a problem (NPA) and not others. Then, all the facilities granted by a bank to a borrower will have to be treated as NPA and not the facility which has become irregular.

For NPA classification, auditors need to examine whether all loans of the borrower have been tacked under one customer ID by the bank and also are aggregated properly with respective of being given from various location/divisions of the bank so as to ensure that all the facilities of the borrower are classified as NPA if one of the facilities get classified as NPA as required by RBI guidelines.

Exception to Borrower-wise Classification

- 4.22 The bills discounted under LC favouring a borrower may not be classified as a non-performing asset (NPA), when any other facility granted to the borrower is classified as NPA. However, in case documents under LC are not accepted on presentation or the payment under the LC is not made on the due date by the LC issuing bank for any reason and the borrower does not immediately make good the amount disbursed as a result of discounting concerned bills, the outstanding bills discounted will immediately be classified as NPA with effect from the date when the other facilities has been classified as NPA.

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If the debits arising out of devolvement of letters of credit or invoked guarantees are parked in a separate account, the balance outstanding in that account also should be treated as a part of the borrower's principal operating account for the purpose of application of prudential norms on income recognition, asset classification and provisioning.

Advances under Consortium Arrangements

- 4.23 Asset classification of accounts under consortium should be based on the **record of recovery of the individual member banks** and other aspects having a bearing on the recoverability of the advances. Where the remittances by the borrower under consortium lending arrangements are pooled with one bank and/or where the bank receiving remittances is not parting with the share of other member banks, the account will be treated as not serviced in the books of the other member banks and therefore, be treated as NPA. The banks participating in the consortium should, therefore, arrange to get their share of recovery transferred from the lead bank or get an express consent from the lead bank for the transfer of their share of recovery, to ensure proper asset classification in their respective books.

Erosion in the Value of Security/ Frauds Committed by Borrowers

- 4.24 In respect of accounts where there are potential threats for recovery on account of erosion in the value of security or non-availability of security and existence of other factors such as frauds committed by borrowers it will not be prudent that such accounts should go through various stages of asset classification. In cases of such serious credit impairment, the asset should be straightaway classified as doubtful or loss asset as appropriate.

Erosion in the value of securities can be reckoned as significant when the realizable value of the security is less than 50% of the value assessed by the bank or accepted by RBI at the time of last inspection. Such NPAs may be straightaway classified under doubtful category.

In case realizable value of security as assessed above is less than 10% of the outstanding in the borrower account, the existence of security should be ignored, and asset should be classified as loss asset. In such cases the assets should either be written off or fully provided for.

Provisioning Norms in case of Frauds

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4.25 Banks should normally provide for the entire amount due to the bank or for which the bank is liable (including in the case of deposit accounts), immediately upon fraud being detected. While computing the provisioning requirement, banks may adjust financial collateral eligible under Basel III Capital Regulations - Capital Charge for Credit Risk (Standardised Approach), if any, available with them regarding the accounts declared as fraud account. However, to smoothen the effect of such provisioning on quarterly profit and loss, banks have the option to make the provisions over a period, not exceeding four quarters, commencing from the quarter in which the fraud has been detected. Where the bank chooses to provide for the fraud over two to four quarters and this results in the full provisioning being made in more than one financial year, banks should debit 'other reserves' [i.e., reserves other than the one created in terms of Section 17(2) of the Banking Regulation Act 1949] by the amount remaining un-provided at the end of the financial year by credit to provisions. However, banks should proportionately reverse the debits to 'other reserves' and complete the provisioning by debiting profit and loss account, in the subsequent quarters of the next financial year.

Wilful Defaulters

- 4.26 Instructions regarding treatment of Wilful Defaulters are contained in our Master Direction DoR.FIN.REC. No.31/20.16.003/2024-25 dated July 30, 2024, on 'Treatment of Wilful Defaulters and Large Defaulters' (as updated from time to time). Banks are required to strictly adhere to these guidelines.
- 4.27 In addition to these instructions and with a view to ensuring better corporate governance structure in companies and ensuring accountability of independent/professional directors, promoters, auditors, etc. henceforth, the following prudential measures will be applicable.
- 4.28 The provisioning in respect of existing loans/exposures of banks to companies having director/s (other than nominee directors of government/financial institutions brought on board at the time of distress), whose name/s appear more than once in the list of wilful defaulters, will be 5% in cases of standard accounts; if such account is classified as NPA, then such accounts will be exposed to higher/accelerated provisions as contained in the Master Direction mentioned at para no 4.24 above.

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Advances to Primary Agricultural Credit Societies (PACS)/Farmers' Service Societies (FSS) ceded to Commercial Banks

- 4.29 In respect of agricultural advances as well as advances for other purposes granted by banks to PACS/ FSS under the on-lending system, only that particular credit facility granted to PACS/ FSS which is in default for a period of two crop seasons in case of short duration crops and one crop season in case of long duration crops, as the case may be, after it has become due will be classified as NPA and not all the credit facilities sanctioned to a PACS/ FSS. The other direct loans & advances, if any, granted by the bank to the member borrower of a PACS/ FSS outside the on-lending arrangement will become NPA even if one of the credit facilities granted to the same borrower becomes NPA.

Advances against Term Deposits, NSCs, KVPs/IVPs, etc.

- 4.30 Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and life policies need not be treated as NPAs, provided adequate margin is available in the accounts. Advances against gold ornaments, government securities and all other securities are not covered by this exemption.

Loans with Moratorium for Payment of Interest

- 4.31 In the case of bank finance given for industrial projects or for agricultural plantations, etc., where moratorium is available for payment of interest, payment of interest becomes 'due' only after the moratorium or gestation period is over. Therefore, such amounts of interest do not become overdue and hence do not become NPA, with reference to the date of debit of interest. They become overdue after due date for payment of interest, if uncollected.

In the case of housing loan or similar advances granted to staff members where interest is payable after recovery of principal, interest need not be considered as overdue from the first quarter onwards. Such loans/advances should be classified as NPA only when there is a default in repayment of instalment of principal or payment of interest on the respective due dates.

Agricultural Advances

- 4.32 A loan granted for short duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for two crop seasons.

A loan granted for long duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season. For these guidelines, “long duration” crops would be crops with crop season longer than one year and crops, which are not “long duration” crops, would be treated as “short duration” crops. The crop season for each crop, which means the period up to harvesting of the crops raised, would be as determined by the State Level Bankers’ Committee (SLBC) in each State. Depending upon the duration of crops raised by an agriculturist, the above NPA norms would also be made applicable to agricultural term loans availed of by him.

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

In such cases of conversion or re-schedule, the term loan as well as fresh short-term loan may be treated as current dues and need not be classified as NPA. The asset classification of these loans would thereafter be governed by the revised terms & conditions and would be treated as NPA if interest and/or instalment of principal remains overdue for two crop seasons for short duration crops and for one crop season for long duration crops. While fixing the repayment schedule in case of rural housing advances granted to agriculturists under Indira Awas Yojana / Pradhan Mantri Gram Awas Yojana and Golden Jubilee Rural Housing Finance Scheme, banks should ensure that the interest/instalment payable on such advances are linked to crop cycles.

Government Guaranteed Advances

- 4.33 The credit facilities backed by guarantee of the Central Government though overdue may be treated as NPA only when the Government repudiates its guarantee when invoked. This exemption from classification of Government guaranteed advances as NPA is not for

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the purpose of recognition of income. The requirement of invocation of guarantee has been delinked for deciding the asset classification and provisioning requirements in respect of State Government guaranteed exposures.

Projects under Implementation

- 4.34 For all projects financed by the FIs/ banks the 'Date of Completion' and the 'Date of Commencement of Commercial Operations' (DCCO), of the project should be clearly spelt out at the time of financial closure of the project and the same should be formally documented. These should also be documented in the appraisal note by the bank during sanction of the loan.

Detailed guidelines regarding classification, provisioning and income recognition for Deferment of Projects under Implementation as well as bifurcation between 'Infrastructure Projects' and 'Non-Infrastructure Projects' given in various RBI circulars should be followed.

Post-shipment Supplier's Credit

- 4.35 In respect of post-shipment credit extended by the banks covering export of goods to countries for which the Export Credit Guarantee Corporation's (ECGC) cover is available, EXIM Bank has introduced a guarantee-cum-refinance programme whereby, in the event of default, EXIM Bank will pay the guaranteed amount to the bank within a period of 30 days from the day the bank invokes the guarantee after the exporter has filed claim with ECGC. Accordingly, to the extent payment has been received from the EXIM Bank, the advance may not be treated as a non-performing asset for asset classification and provisioning purposes.

Export Project Finance

- 4.36 In respect of export project finance, there could be instances where the actual importer has paid the dues to the bank abroad but the bank in turn is unable to remit the amount due to political developments such as war, strife, UN embargo, etc. In such cases, where the lending bank is able to establish through documentary evidence that the importer has cleared the dues in full by depositing the amount in the bank abroad before it turned into NPA in the books of the bank, but the importer's country is not allowing the funds to be remitted due to political or other reasons, the asset classification may be made after a period of one

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year from the date the amount was deposited by the importer in the bank abroad.

Takeout Finance

- 4.37 Takeout finance is the product emerging in the context of the funding of long-term infrastructure projects. Under this arrangement, the institution/the bank financing infrastructure projects will have an arrangement with any financial institution for transferring to the latter the outstanding in respect of such financing in their books on a predetermined basis. In view of the time-lag involved in taking-over, the possibility of a default in the meantime cannot be ruled out. The norms of asset classification will have to be followed by the concerned bank/financial institution in whose books the account stands as balance sheet item as on the relevant date. If the lending institution observes that the asset has turned NPA based on the record of recovery, it should be classified accordingly. The lending institution should not recognise income on accrual basis and account for the same only when it is paid by the borrower/ taking over institution (if the arrangement so provides). However, the taking over institution, on taking over such assets, should make provisions treating the account as NPA from the actual date of it becoming NPA even though the account was not in its books as on that date.

Credit Card Accounts

- 4.38 In credit card accounts, the amount spent is billed to the card users through a monthly statement with a definite due date for repayment. Banks give an option to the card users to pay either the full amount or a fraction of it, i.e., minimum amount due, on the due date and roll-over the balance amount to the subsequent months' billing cycle.

A credit card account will be treated as non-performing asset if the minimum amount due, as mentioned in the statement, is not paid fully within 90 days from the next statement date. The gap between two statements should not be more than a month. Banks should follow this uniform method of determining over-due status for credit card accounts while reporting to credit information companies and for the purpose of levying of penal charges, viz. late payment charges, etc., if any.

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Writing off NPAs

- 4.39 In terms of Section 43(D) of the Income Tax Act, 1961, income by way of interest in relation to such categories of bad and doubtful debts as may be prescribed having regard to the guidelines issued by the RBI in relation to such debts, shall be chargeable to tax in the previous year in which it is credited to the bank's profit and loss account or received, whichever is earlier.
- 4.40 This stipulation is not applicable to provisioning required to be made as indicated above. In other words, amounts set aside for making provision for NPAs as above are not eligible for tax deductions.

Therefore, the banks should either make full provision as per the guidelines or write-off such advances and claim such tax benefits as are applicable, by evolving appropriate methodology in consultation with their auditors/tax consultants. Recoveries made in such accounts should be offered for tax purposes as per the rules.

Write-off at Head Office Level

- 4.41 Banks may write-off advances at Head Office level, even though the relative advances are still outstanding in the branch books. However, it is necessary that provision is made as per the classification accorded to the respective accounts. In other words, if an advance is a loss asset, 100 percent provision will have to be made there for.
- 4.42 Banks are custodians of public deposits and are therefore expected to make all efforts to protect the value of their assets. Banks are required to extinguish all available means of recovery before writing off any account fully or partly.

It is observed that some banks are resorting to technical write off accounts, which reduces incentives to recover. Banks resorting to partial and technical write-offs should not show the remaining part of the loan as standard asset.

With a view to bring in more transparency, henceforth banks should disclose full details of write offs, including separate details about technical write offs, in their annual financial statements as per the format prescribed in the Annex III – 4(a) of the Master Direction on Financial Statements - Presentation and Disclosures dated August 30, 2021, as updated from time to time.

NPA Management – Requirement of Effective Mechanism and Granular Data

- 4.43 Asset quality of banks is one of the most important indicators of their financial health. Banks should, therefore put in place a robust MIS mechanism for early detection of signs of distress at individual account level as well as at segment level (asset class, industry, geographic, size, etc.). Such early warning signals should be used for putting in place an effective preventive asset quality management framework, including a transparent restructuring mechanism for viable accounts under distress within the prevailing regulatory framework, for preserving the economic value of those entities in all segments.

As part of effective monitoring of financial health of their loan portfolio, Bankers shall recognise incipient stress in loan accounts, immediately on default, by classifying such assets as special mention accounts (SMA) as per the following categories.

SMA	Sub-categories	Basis for classification – Principal or interest payment or any other amount wholly or partly overdue between
SMA-0		Up to 30 days
SMA-1		More than 30 days and up to 60 days-
SMA-2		More than 60 days and up to 90 days

In the case of revolving credit facilities like cash credit/overdraft, the SMA sub-categories will be as follows:

SMA Sub-categories	Basis for classification – Outstanding balance remains continuously more than the sanctioned limit or drawing power, whichever is lower, for a period of:
SMA-1	More than 30 days and up to 60 days
SMA-2	More than 60 days and up to 90 days

Classification of borrower accounts as SMA as well as NPA shall be done as part of day-end process for the relevant date and the SMA or NPA classification date shall be the calendar date for which the day end process is run. In other words, the date of SMA/NPA shall reflect the

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asset classification status of an account at the day-end of that calendar date.

General Principles and Prudential Norms for Restructured Advances

- 4.44 The following principles and prudential norms are applicable to all advances including the borrowers, who are eligible for special regulatory treatment for asset classifications:

Banks may restructure the accounts classified under 'standard', 'substandard' and 'doubtful' categories.

Banks cannot reschedule/ restructure/ renegotiate borrower accounts with retrospective effect. While a restructuring proposal is under consideration, the usual asset classification norms would continue to apply.

The process of re classification of an asset should not stop merely because restructuring proposal is under consideration.

Normally, restructuring cannot take place unless alteration/ changes in the original loan agreement are made with the formal consent/ application of the debtor. However, the process of restructuring can be initiated by the bank in deserving cases subject to customer agreeing to the terms and conditions.

No account will be taken up for restructuring by the banks unless the financial viability is established and there is a reasonable certainty of repayment from the borrower as per the terms of restructuring package.

While the borrowers indulging in frauds and malfeasance will continue to remain ineligible for restructuring, banks may review the reasons for classification of the borrowers as wellful defaulters. BIFR cases are not eligible for restructuring without their express approval.

Government Debt Relief Schemes (DRS)

- 4.45 Banks participating as lenders under Debt Relief Schemes (DRS) announced by State Governments shall comply with the guidelines contained in Annex-1 of the circular on Government Debt Relief Schemes (DRS) dated December 31, 2024.

Bank Loans for Financing Promoters' Contribution

- 4.46 In terms of extant instructions on Bank Loans for Financing Promoters Contribution as consolidated in our Master Circular

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DBOD.No.Dir.BC.16/13.03.00/2014-15 dated July 1, 2015 on 'Loans and Advances – Statutory and Other Restrictions', the promoters' contribution towards the equity capital of a company should come from their own resources and banks should not normally grant advances to take up shares of other companies.

- 4.47 It has been decided that banks can extend finance to 'specialized' entities established for acquisition of troubled companies subject to the general guidelines applicable to advances against shares/debentures/bonds as contained in the above-mentioned Master Circular and other regulatory and statutory exposure limits. The lenders should, however, assess the risks associated with such financing and ensure that these entities are adequately capitalized, and debt equity ratio for such entity is not more than 3.1.

Credit Risk Management

- 4.48 Banks are advised that they should strictly follow the credit risk management guidelines contained in our circular DBOD.No.BP.(SC).BC.98/21.04.103/99 dated October 7, 1999 on 'Risk Management Systems in Banks', and DBOD.No.BP.520/21.04.103/2002-03 dated October 12, 2002 on 'Guidance Notes on Management of Credit Risk and Market Risk'.
- 4.49 It is reiterated that lenders should carry out their independent and objective credit appraisal in all cases and must not depend on credit appraisal reports prepared by outside consultants, especially the in-house consultants of the borrowing entity.
- 4.50 Banks shall review their extant sectoral exposure limits for consumer credit and put in place, if not already there, Board approved limits in respect of various sub-segments under consumer credit as may be considered necessary by the Boards as part of prudent risk management. Limits shall be prescribed for all unsecured consumer credit exposures. The limits so fixed shall be strictly adhered to and monitored on an ongoing basis by the Risk Management Committee.

Registration of Transactions with CERSAI

- 4.51 Banks shall register the transactions relating to Securitisation, Asset Reconstruction and Security Interest as per the provisions of SARFAESI Act and SARFAESI (CERSAI) Rules, as amended time to time.

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Board Oversight

- 4.52 The Board of Directors of banks should take all necessary steps to arrest the deteriorating asset quality in their books and should focus on improving the credit risk management system. Early recognition of problems in asset quality and resolution envisaged in these guidelines requires the lenders to be proactive and make use of Central Repository of Information on Large Credits (CRILC).

Chapter 5

Internal Control and Vigil Mechanism

Internal Control

- 5.1 Adequate internal controls within banking organisations must be supplemented by an effective internal/concurrent audit function that independently evaluates the control systems within the organisation. Concurrent audit is part of the ongoing monitoring of the bank's system of internal controls, because concurrent audit provides an independent assessment of the adequacy of and compliance with the bank's established policies and procedures.
- 5.2 The concurrent audit function assists senior management and the Board of Directors in the efficient and effective discharge of their responsibilities as described above. Banks should have in place adequate internal audit coverage to verify that operating policies and procedures have been implemented effectively. The Board (either directly or indirectly through its Audit Committee) should ensure that the scope and frequency of the audit programme is appropriate to the risk exposures.
- 5.3 RBI Master Directions (Frauds - Classification and Reporting by commercial banks and select FIs) Directions 2016 (Ref.DBS.CO.CFMC.BC.No.1/23.04.001/2016-17) dated July 01, 2016 (Updated as on July 03, 2017) have been superseded by Master Directions on Fraud Risk Management in Commercial Banks (including Regional Rural Banks) and All India Financial Institutions Circular No. RBI/DOS/2024-25/118: DOS.CO.FMG.SEC.No.5/23.04.001/2024-25 dated 15th July 2024.
- 5.4 These Directions are issued with a view to providing a framework to banks for prevention, early detection and timely reporting of incidents of fraud to Law Enforcement Agencies (LEA's), Reserve Bank of India (RBI) and NABARD and dissemination of information by RBI and matters connected with or incidental thereto.

Governance Structure in banks for Fraud Risk Management

- 5.5 There shall be a Board approved Policy on fraud risk management delineating roles and responsibilities of Board / Board Committees and Senior Management of the bank. The Policy shall also incorporate measures for ensuring compliance with principles of natural justice in a time-bound manner, including issue of Show Cause Notices (SCN's) on the concerned persons, promoters or executives with complete particulars about the nature of transactions, etc., giving them opportunity to give their submissions, examining the same and passing reasoned orders.

Banks shall have a well laid out system for issuance of SCN and examination of the responses/ submissions made by the Persons /Entities prior to declaring such Persons/ Entities as fraudulent.

A reasoned Order shall be served on the Persons/ Entities conveying the decision of the bank regarding declaration/ classification of the account as fraud or otherwise. Such Order(s) must contain relevant facts/ circumstances relied upon, the submission made against the SCN and the reasons for classification as fraud or otherwise.

The Fraud Risk Management Policy shall be reviewed by the Board at least once in three years, or more frequently, as may be prescribed by the Board.

Special Committee of the Board for Monitoring and Follow-up of cases of Frauds

- 5.6 Banks shall constitute a Committee of the Board to be known as 'Special Committee of the Board for Monitoring and Follow-up of cases of Frauds' (SCBMF) with a minimum of three members of the Board, consisting of a whole-time director and a minimum of two independent directors/ non-executive directors. The Committee shall be headed by one of the independent directors/ non-executive directors.

SCBMF shall oversee the effectiveness of the fraud risk management in the bank. SCBMF shall review and monitor cases of frauds, including root cause analysis, and suggest mitigating measures for strengthening the internal controls, risk management framework and minimising the

incidence of frauds. The coverage and periodicity of such reviews shall be decided by the Board of the bank.

Banks shall set-up an appropriate organisational structure for institutionalisation of fraud risk management within their overall risk management functions/ Department. A senior official in the rank of at least a General Manager or equivalent shall be responsible for monitoring and reporting of frauds. Banks shall put in place a transparent mechanism to ensure that Whistle Blower complaints on possible fraud cases/ suspicious activities in account(s) are examined and concluded appropriately under their Whistle Blower Policy.

Early Detection of Frauds – Framework for Early Warning Signals (EWS) and Red Flagging of Accounts (RFA)

- 5.7 Banks shall have a framework for Early Warning Signals (EWS) and Red Flagging of Accounts (RFA) under the overall Fraud Risk Management Policy approved by the Board. A Red Flagged Account is one where suspicion of fraudulent activity is thrown up by the presence of one or more EWS indicators, alerting/ triggering deeper investigation from potential fraud angle and initiating preventive measures by the banks.
- 5.8 The EWS/ RFA Framework shall provide for, among others:
- (i) A system of robust EWS which is integrated with Core Banking Solution (CBS) or other operational systems.
 - (ii) Initiation of remedial action on alerts /triggers from EWS System in a timely manner.
 - (iii) Periodic review of credit sanction and monitoring processes, internal controls and systems; and
 - (iv) Effective use of Central Repository of Information on Large Credits (CRILC) database and the Central Fraud Registry (CFR).

EWS / RFA Framework for Credit Facilities / Loan Accounts

5.9 EMS/ RFA Framework for Credit Facilities / Loan Accounts is as follows:

- (i) Development of EWS System -To include quantitative and Qualitative information to make framework robust and effective by capturing the

Internal Control and Vigil Mechanism

transactional data of the accounts from the system, financial performance of the borrower, Market Intelligence, conduct of borrowers, etc.

- (ii) Data Analytics and Market Intelligence (MI) - Banks shall set up a dedicated Data Analytics and MI Unit keeping in view their size, complexity, business mix, risk profile, etc. Such Unit shall facilitate collection and processing of relevant information to enable an early detection and prevention of potentially fraudulent activities.
- (iii) Generation of EWS alert(s)/ trigger(s) shall necessitate examination whether the account needs to be red flagged and consequently, investigation from potential fraud angle.
- (iv) An account meeting CRILC threshold to be reported to RBI within 7 days of being identified as RFA.

Further Action of Red Flagged Accounts (RFA's)

5.10 Further Actions to be taken for Red Flagged Accounts (RFA's) are as follows:

- (i) Banks shall frame a policy on engagement of external auditors covering aspects such as due diligence, competency and track record of the auditors, among others. Further, the contractual agreement with the auditors shall, inter alia, contain suitable clauses on timeline for completion of the audit of RFA and submission of audit report to the bank within a specified time limit, as approved by the Board.
- (ii) The loan agreement with the borrower shall contain clauses for conduct of such audit at the behest of lender(s) consequent upon red flagging of the account. In cases where the audit report submitted remains inconclusive or is delayed due to non-cooperation by the borrower, banks shall conclude on status of the account as a fraud or otherwise based on the material available on their record and their own internal investigation/ assessment in such cases.
- (iii) The decision to classify any account, either standard or NPA, as a red-flagged account shall be at the individual bank level and such bank(s) shall report the status of the accounts on the Reserve Bank's CRILC platform immediately (not later than seven days from date of classification as red-flagged account).

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- (iv) Once an account has been red-flagged, the entire process of classification of the account as fraud or removal of red-flagged status shall ordinarily be completed within 180 days from the date of first reporting of the account as red- flagged on the CRILC platform. Cases remaining in red-flagged status beyond 180 days shall be reported to the SCBMF for review with adequate reasoning /justification thereof. Such cases shall also be subject to supervisory review by the Reserve Bank.
- (v) In case an account is identified as a fraud by any bank, the borrower accounts of other group companies, in which one or more promoter(s)/ whole-time director(s) are common, shall also be subjected to examination by banks concerned from fraud angle under these Directions.
- (vi) In cases where Law Enforcement Agencies (LEAs) have Suo moto-initiated investigation involving a borrower account, bank/s shall immediately red-flag the account and follow the usual process for classification of account as fraud and complete the same within the stipulated period as specified at Para (iv) above.

Penal Measures

5.11 Penal Measures for Persons / Entities classified and reported as fraud by banks and Entities and Persons associated with such Entities are as follows:

- (i) Persons/ Entities classified and reported as fraud by banks and Entities and Persons associated with such Entities, shall be debarred from raising of funds and / or seeking additional credit facilities from financial entities regulated by RBI, for a period of five years from the date of full repayment of the defrauded amount / settlement amount agreed upon in case of a compromise settlement.
- (ii) Lending to such Persons/ Entities, being commercial decisions, the lending banks shall have the sole discretion to entertain or decline such requests for credit facilities after the expiry of the mandatory cooling period as mentioned at Para (i) above.

Reporting of Frauds to Law Enforcement Agencies (LEA's)

5.12 Reporting of Frauds to law enforcement agencies is as follows:

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- (i) Private Sector and Foreign Banks should report Frauds up to Rs 1 cr to State/UT Police Authorities. Frauds more than Rs 1 cr to be additionally reported to Serious Fraud Investigation Office (SFIO). Details of Fraud are also to be reported to SFIO in Fraud Monitoring Report (FMR) Format.
- (ii) In respect of Public Sector Banks (PSB's) and Regional Rural Banks (RRB'S) Frauds up to Rs 6 Crs. are to be reported to State/UT Police authorities, while Frauds more than Rs 6 Crs. are to be reported to Central Bureau of Investigations (CBI).

Reporting of Frauds to RBI through Fraud Monitoring Report (FMR)

5.13 Reporting of Frauds to RBI through Fraud Monitoring Report (FMR) is as follows:

- (i) To ensure uniformity and consistency while reporting incidents of fraud to RBI through Fraud Monitoring Returns (FMRs) using online portal, banks shall choose the most appropriate category from any one of the following:
 - (a) Misappropriation of funds and criminal breach of trust.
 - (b) Fraudulent encashment through forged instruments.
 - (c) Manipulation of books of accounts or through fictitious accounts, and conversion of property.
 - (d) Cheating by concealment of facts with the intention to deceive any person and cheating by impersonation.
 - (e) Forgery with the intention to commit fraud by making any false documents/electronic records.
 - (f) Wilful falsification, destruction, alteration, mutilations of any book, electronic record, paper, writing, valuable security or account with intent to defraud.
 - (g) Fraudulent credit facilities extended for illegal gratification.
 - (h) Cash shortages on account of frauds.
 - (i) Fraudulent transactions involving foreign exchange.
 - (j) Fraudulent electronic banking / digital payment related transactions committed on banks; and

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- (k) Other type of fraudulent activity not covered under any of the above.
- (ii) Central Fraud Registry (CFR)- Banks shall put in place systems and procedures to ensure that the information available in Central Fraud Registry (CFR) is used for credit risk and fraud risk management effectively.
- (iii) Banks are required to report payment system related disputed / suspected or attempted fraudulent transactions to Central Payments Fraud Information Registry (CPFIR), maintained by RBI. However, such transactions, if subsequently concluded as fraud committed on bank(s), shall invariably be reported through FMR to be reflected in CFR.

Modalities of Reporting Incidents of Fraud to RBI

5.14 Modalities of Reporting incidents of frauds to RBI are as follows:

- (i) Banks shall furnish FMR in individual fraud cases, irrespective of the amount involved, immediately, but not later than 14 days from the date of classification of an incident / account as fraud.
- (ii) Incidents of fraud at overseas branches of Indian banks shall also be reported to the concerned overseas LEAs in accordance with the relevant laws / regulations of the host countries.
- (iii) Banks shall also report frauds perpetrated in their group entities to RBI separately, if such entities are not regulated / supervised by any financial sector regulatory / supervisory authority. However, in case of overseas banking group entity of Indian banks, the parent bank shall also report incidents of fraud to RBI. The group entities will have to comply with the principles of natural justice before declaration of fraud.
- (iv) Banks shall adhere to the timeframe prescribed in these Master Directions for reporting of fraud cases to RBI. Banks shall examine and fix staff accountability for delays in identification of fraud cases and in reporting to RBI.
- (v) While reporting frauds, banks shall ensure that persons / entities who /which are not involved / associated with the fraud are not reported in the FMR.

Closure of Fraud Cases Reported to RBI

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5.15 Closure of Fraud Cases Reported to RBI is as follows:

- (i) Banks shall close fraud cases using 'Closure Module' where the actions as stated below are complete:
 - (a) The fraud cases pending with LEAs/ Court are disposed of; and
 - (b) The examination of staff accountability has been completed.
- (ii) Banks are allowed, for limited statistical/ reporting purposes, to close those reported fraud cases involving amount up to ₹1 crore where examination of staff accountability and disciplinary action, if any, have been taken and:
 - (a) The investigation is going on or charge-sheet has not been filed in the Court by LEA for more than three years from the date of registration of First Information Report (FIR); or
 - (b) The charge-sheet is filed by the LEAs in trial court and the trial in the court has not commenced or is pending before the court for more than three years from the date of registration of FIR.
- (iii) In all closure cases of reported frauds, banks shall maintain details of such cases for examination by auditors.

Cheque Related Frauds - Reporting to LEAs and RBI / NABARD

5.16 Procedure for reporting Cheque related frauds to LEAs and RBI/ NABARD is as follows:

To ensure uniformity and avoid duplication, reporting of frauds involving forged instruments, including fake / forged instruments sent in clearing in respect of truncated instruments, shall continue to be done by the paying banker and not by the presenting banker. In such cases the presenting bank shall immediately handover the underlying instrument to the drawee / paying bank, as and when demanded, to enable them to inform LEAs for investigation and further action under law and to report the fraud to RBI.

However, in the case of presentment of an instrument which is genuine but payment has been made to a person who is not the true owner; or where the amount has been credited before realisation and subsequently the instrument is found to be fake / forged and returned by the paying bank, the presenting bank which is defrauded or is put to loss by paying the amount before realisation of the instrument shall file the fraud report with the RBI and inform

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the LEAs for investigation and further action under law.

Treatment of Accounts classified as Fraud and sold to other Lenders/ Asset Reconstruction Companies (ARCs)

5.17 Treatment of Accounts classified as Fraud and sold to other Lenders/ Asset Reconstruction Companies (ARCs) is as follows:

Banks shall complete the investigation from fraud angle before transferring the loan account / credit facility to other lenders / ARCs. In cases where banks conclude that a fraud has been perpetrated in the account, they shall report it to RBI / NABARD before selling the accounts to another lenders/ARC's.

Role of Auditors

5.18 Role of Auditors are as follows:

- (i) During the course of the audit, auditors may come across instances where the transactions in the account or the documents point to the possibility of fraudulent transactions in the account. In such a situation, the auditor should immediately bring it to the notice of the senior management and if necessary, to the Audit Committee of the Board (ACB) of the bank for appropriate action.
- (ii) Internal /Concurrent Audit in banks shall cover controls and processes involved in prevention, detection, classification, monitoring, reporting, closure and withdrawal of fraud cases, and weaknesses observed in the critical processes in the fraud risk management framework of the bank.

Indicative List of Suspicious Activities

5.19 Following is an indicative list of suspicious activities:

(A) Activities not consistent with the customer's business

- (i) Corporate accounts where deposits or withdrawals are, primarily in cash rather than in cheques.
- (ii) Corporate accounts where foreign inward remittances and any other means are received from/made to sources apparently unconnected with the corporate business activity /dealings.
- (iii) Unusual applications for DD/ TT/ PO against cash.
- (iv) Accounts with large volume of credits through DD/ TT/PO whereas the

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nature of business does not justify such credits.

- (v) Accounts with high volume of transactions, with low closing balance.
- (vi) Retail deposit of many cheques but rare withdrawals for daily operations.

(B) Attempts to Avoid Reporting/ Record-keeping Requirements

- (i) A customer who is reluctant to provide information needed for a mandatory report, to have the report filed or to proceed with a transaction after being informed that the report must be filed.
- (ii) Any individual or group that coerces/induces or attempts to coerce/induce bank employee and does not file any reports or any other forms.
- (iii) An account where there are several cash deposits/ withdrawals below a specified threshold level to avoid filing of reports that may be necessary in case of transaction above the threshold limit, as the customer intentionally splits the transaction into smaller amounts for the purpose of avoiding the threshold limit.

(C) Unusual activities

- (i) An account of a customer who does not resides/have office near the branch even though there are bank branches near his residence/office.
- (ii) A customer who often visits the safe deposit area immediately before making cash deposits -especially deposits just under the threshold level.
- (iii) An account that has frequent deposits of large amounts of currency bearing the labels of other banks.
- (iv) Funds coming from the list of countries/centres which are known for money laundering.

(D) Customer who provides insufficient or suspicious information

- (i) A customer/company who is reluctant to provide complete information regarding the purpose of the business, prior banking relationships, officers or directors, or its locations. In this case account need not be opened.
- (ii) A customer/company who is reluctant to reveal details about its

activities or to provide financial statements.

- (iii) A customer who has no record of past or present employment but makes frequent large transactions.

(E) Certain suspicious funds transfer activities

- (i) Sending or receiving frequent or large volumes of cross border remittances.
- (ii) Receiving large remittances from various centres and remitting the consolidated amount to different account centre on the same day, leaving minimum balance in the account.

Early Warning Signals

5.20 RBI Master Directions on Fraud Risk Management issued on 15 July'2024 mandated banks to identify early warning signals for credit frauds and non – credit frauds. Banks shall use these EWS for continuous monitoring of fraud risk in various transactions. The illustrative fraud risk indicators which the concurrent auditor may consider are as given below:

- (a) Default in undisputed payment to the statutory bodies as declared in the Annual Report.
- (b) Bouncing of high value cheques:
 - (1) Frequent change in the scope of the project to be undertaken by the borrower.
 - (2) Foreign bills remaining outstanding with the bank for a long time and tendency for bills to remain overdue.
 - (3) Delay observed in payment of outstanding dues.
 - (4) Frequent invocation of BGs and devolvement of LCs.
 - (5) Under insured or over insured inventory.
 - (6) Invoices devoid of TAN and other details.
 - (7) Dispute on the title of collateral securities.
 - (8) Funds coming from other banks to liquidate the outstanding loan amount unless in normal course.

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- (9) In merchanting trade, import leg not revealed to the bank.
- (10) Request received from the borrower to postpone the inspection of the godown for flimsy reasons.
- (11) Funding of the interest by sanctioning additional facilities.
- (12) Exclusive collateral charged to a few lenders without NOC of existing charge holders.
- (13) Concealment of certain vital documents like master agreement, insurance coverage.
- (14) Floating front / associate companies by investing borrowed money.
- (15) Critical issues highlighted in the Stock Audit report.
- (16) Liabilities appearing in ROC search report, not reported by the borrower in its annual report.
- (17) Frequent request for general purpose loans.
- (18) Frequent ad hoc sanctions.
- (19) Not routing of sales proceeds through consortium/ member bank/lenders to the company.
- (20) LCs issued for local trade / related party transactions without underlying trade transaction.
- (21) High value RTGS payment to unrelated parties.
- (22) Heavy cash withdrawal in loan accounts.
- (23) Non submission of original bills for verification upon request.
- (24) Significant movements in inventory, disproportionately differing vis-a- vis change in the turnover.
- (25) Significant movements in receivables, disproportionately differing vis- a-vis change in the turnover.
- (26) Disproportionate change in other current assets.
- (27) Significant increase in working capital borrowing as percentage of turnover.
- (28) Increase in Fixed Assets, without corresponding increase in long term sources (when project is implemented).

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- (29) Increase in borrowings, despite huge cash and cash equivalents in the borrower's balance sheet.
- (30) Frequent change in accounting period and/or accounting policies.
- (31) Costing of the project which is in wide variance with standard cost of installation of the project.
- (32) Claims not acknowledged as debt high.
- (33) Substantial increase in unbilled revenue year after year.
- (34) Large number of transactions with inter-connected companies and large outstanding from such companies.
- (35) Substantial related party transactions.
- (36) Material discrepancies in the annual report.
- (37) Significant inconsistencies within the annual report (between various sections).
- (38) Poor disclosure of materially adverse information and no qualification by the statutory auditors.
- (39) Raid by Income tax /sales tax/ central excise duty official.
- (40) Significant reduction in the stake of promoter / director or increase in the encumbered shares of promoter/director.
- (41) Resignation of the key personnel and frequent changes in the management.

Also refer to extant circulars on related to this and ICAI's Publication on EWS.

Relevant RBI circulars to be referred by the Concurrent Auditors

1. **Central Payments Fraud Information Registry – Migration of Reporting to DAKSH**
RBI/2022-23/158CO.DPSS.OVRST.No.S1619/06-08-005/2022-2023
December 26, 2022
2. **Master Circular – Detection and Impounding of Counterfeit Notes**
RBI/2025-26/132 DCM (FNVD)/G4/16.01.05/2025-26 dated 01-04-2025
3. **Increasing Instances of Payment Frauds – Enhancing Public Awareness Campaigns Through Multiple Channels**

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RBI/2019-20/256DPSS.CO.OD. No.1934/06.08.005/2019-20 June 22, 2020

4. Guidance Note on Operational Risk Management and Operational Resilience Circular No. RBI/2024-25/31 DOR.ORG.REC.21/14.10.001/2024-25 dated 30-04-2025.
5. Frequently Asked Questions (FAQs) Master Directions on Fraud Risk Management in Regulated Entities (REs), 2024, dated 22nd April 2025.

Introduction of Prevention of Money Laundering Act, 2002 (PMLA)

- (a) Government of India enacted a Law named "Prevention of Money Laundering Act, 2002 in the year 2005.
- (b) This Act is being aimed to prevent Money Laundering and other Financial Crimes.
- (c) Through this Act Government of India prevent and detect the Money Laundering Activities and prosecute the persons who have involved in all those activities. Apart from that the Act provides to confiscate the properties which have been derived from those activities.
- (d) Money Laundering (ML) is an activity that converts proceeds of crime funds into legitimate assets.
- (e) To check and control the ML activities, the Banks, FI and other Designated entities must follow the following:
 - To maintain records of all the Financial Transactions.
 - To verify the identity of their customers.
 - To report suspicious transactions to Financial Intelligence Unit (FIU).
- (f) ML and Financial crimes in India are covered through PMLA.
- (g) PMLA created Law to control and prevent ML and Financial Crimes.
- (h) ML and Financial crimes are tried under Special Courts, which have been established under the PMLA, 2002.
- (i) PMLA is under the control of Department of Revenue of Ministry of Corporate Affairs.

Concurrent Auditors are advised to understand the Provisions stated in **Prevention of Money Laundering Act, 2002** and the Rules stated in **Prevention of Money Laundering (Maintenance of Records) Rules 2005.**

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- The Matters submitted are here only for your reference and easy understanding of the provisions of PMLA.
- Members are also kindly requested to refer latest guidelines on PMLA Rules, 2005 in Circular Number DGA/Tech/Misc/26/2022-TECH-O/o DG-DGA-HQ-DELHIDGA/Tech/Misc/26/2022-TECH-O/o DG-DGA-HQ-DELHI I/1575014/2023 dated 29-11-2023 issued by DIRECTORATE GENERAL OF AUDIT INDIRECT TAXES & CUSTOMS.

Chapter 6

Treasury and Investment Portfolio of Banks

6.1 Fund and investment management are one of the most important and sensitive functions of the bank. The management of the liquidity and investment portfolio of the bank will be under the responsibility of a committee called as “Funds Management and Investment Committee”.

The functions of treasury include:

- (i) Fund management for the bank being central pool of funds for the bank.
- (ii) Maintenance of Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR).
- (iii) Investment functions of the bank.
- (iv) Risk management.
- (v) Liquidity management.
- (vi) Asset Liability Management.
- (vii) Participation in forex, money and securities markets.
- (viii) Proprietary trading.
- (ix) Global cash management.
- (x) Managing the cost of funds- Net Interest Income, Net Interest Margin, Return on Assets.
- (xi) Monitoring the rating migrations.

6.2 Concurrent audit of Treasury and Investment Portfolio of Banks is very important for ensuring compliance, risk management and operational efficiency.

6.3 Key consideration in audit of investments:

1. Regulatory Compliance: Ensure adherence to RBI, SEBI and other regulator's guidelines

2. Risk Assessment: Whether market risk, credit risk and liquidity risk associated with investment portfolio properly assessed by auditee.
3. Internal Controls: Assess the effectiveness of internal controls in managing treasury operations.
4. Transaction Review: Verify accuracy and legitimacy of treasury transactions.
5. Reporting and Documentation: Ensure timely and accurate reporting and documentation of transactions.

Audit of Treasury Function

- 6.4 As per the RBI directives, all treasury transactions are subjected to concurrent audit either by banks internal auditor or by a firm of chartered accountants and the report is placed before the MD/CEO of the bank on monthly basis.

The major irregularities observed in these reports and the position of compliance thereto may be incorporated in the half yearly review of the investment portfolio.

Banks should undertake a quarterly review (as of June 30, Sep 30, Dec 30 and March 31) of their investment portfolio, which should, apart from other operational aspects of investment portfolio, clearly indicate amendments made to the Investment Policy and certify adherence to laid down internal investment policy and procedures and the Reserve Bank guidelines, and put up the same before their respective Boards within a month, i.e., by end-July, end-October, end – January and end-April.

A copy of the review report put up to the Bank's Board should be forwarded to the Reserve Bank (concerned Regional Office of DBS, RBI) by Aug 15, November 15, Feb 15 and May 15 respectively.

Concurrent auditor must follow the observation given by RBI based on the Review Report submitted.

Treasury Audit Approach

- 6.5 An Illustrative Checklist for audit of Treasury and Investment function has been discussed in following paragraphs:

Investment Policy

The auditor should verify that:

- (i) There is a clear-cut written Investment policy of the bank, duly approved by the Board and that it includes quantitative aspects of investment held in its own portfolio.
- (ii) Investment policy outlining the approach, operations products, limits and processes, accounting, valuation, etc., is very important.
- (iii) Bank regularly reviews its investment policy and incorporates all the latest guidelines issued by the RBI. Banks should undertake a half-yearly review (as of March 31 and September 30) of their investment portfolio, which should, apart from other operational aspects of investment portfolio, clearly indicate amendments made to the Investment Policy and certify adherence to laid down internal investment policy and procedures, and the Reserve Bank guidelines, and put up the same before their respective Boards within a month, i.e., by end-April and end-October. A copy of the review report put up to the Bank's Board should be forwarded to the Reserve Bank (concerned Regional Office of DBS, RBI) by May 15 and November 15, respectively.
- (iv) It ensures per transaction per exposure limit with counter party/ brokers, wherever necessary.
- (v) It ensures compliance of credit exposure of the bank to individual/group of borrowers while processing/ seeking approval for fresh investment. In this regard, Master Circular – Exposure Norms” (RBI/2015-16/70 DBR.No. Dir.BC.12/13.03.00/2015-16 dated July 1, 2015) is important.
- (vi) It ensures compliance of exposure limit to capital market (the aggregate exposure of the bank to the capital markets in all forms has not exceed 40% of its net worth as on March 31 of the previous year and within overall ceiling the banks direct investments should not exceed 20% of its net worth).
- (vii) Holding of shares of any company as pledge, mortgagee or absolute owner in compliance of section 19(2) of Banking Regulation Act, 1949, regarding investment in equity shares (No

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banking company shall hold shares in any company of an amount exceeding 30% of paid-up share capital of that company or 30% of bank's share capital and reserves, whichever is less).

- (viii) Exposure caps for various investment activities:
 - a. Per entity investments under bonds debentures, commercial paper, certificate of deposits.
 - b. Investments in unlisted Non SLR securities- not to exceed 10% of total investments in Non SLR securities as on 31st March of previous year.
 - c. Banks must not invest in unrated non-SLR securities (except infrastructure bonds) and fixing of prudential limits.
 - d. Cap on NON SLR investments.
 - e. Rating migration of the issuers/ issues held in the bank's books and consequent diminution in the portfolio quality.
 - f. Per transaction limit for purchase/sale of shares in the secondary market.
 - g. Aggregate exposure under MFs.
 - h. Exposure limits for Individual borrower and group accounts.
- (ix) Bank has a list of approved brokers for debt/capital market and per broker's exposure limit is maintained.
- (x) Neat structure of front, back and middle offices with clear cut roles, responsibilities, and duties.
- (xi) A clear reporting structure and coordinating plan.
- (xii) Trading policy describing the trading philosophy, objectives, processes, various limits like, cut loss, dealing limits, etc.
- (xiii) Composition of investment portfolio as per RBI guidelines and the depreciation on investments, if any, not provided for.
- (xiv) System relating to unquoted investments in the portfolio and the liquidity of such investments.
- (xv) System and periodicity of concurrent and internal audit/ inspection of investment activities; follow up on such reports.

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- (xvi) System of recording and accounting of income from investments.
- (xvii) System of monitoring of income accrued and due but not received.
- (xviii) System of monitoring matured investments and their timely encashment.
- (xix) Average yield on investments.
- (xx) Cancelled/ amended/ late(C/A/L) booking transactions – complete inventory on these transactions.

Note: Concurrent auditor has to prepare checklist and observe his comments. This area is very important as the Investment decision policy is not correctly taken then the entire Bank is in trouble. Here the Role of Concurrent auditor is very important.

Investment Management

The auditor should verify that:

- (i) Investment portfolio is managed in accordance with investment policy objectives and in such a manner that risk is minimized, and liquidity is ensured. Investment policy objectives are:
 - to comply with statutory policy obligations.
 - to augment the trading profits and overall yield on investments.
 - investments covered under investment policy are SLR securities, Non SLR securities.
- (ii) There is a clear segregation of duties between front office/dealing room, back office and mid office.
- (iii) Rotation of duties of staff is being done at periodic intervals. Authorized dealers must ensure that the staff concerned in the dealing room understands and abides by the Code of Conduct prescribed by FEDAI and FIMMDA.
- (iv) The prudential limits fixed are strictly adhered to by the bank officials.
- (v) The SGL statement is reconciled with bank record on monthly basis.

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- (vi) The dealer is preparing deal slips for each deal which is serially numbered.
- (vii) The dealer is adhering to per day/per transaction exposure limit fixed, as per investment policy.
- (viii) The dealer is reporting all call/notice/term money market deals on NDS and are reported within 15 minutes in NDS, irrespective of the size of the deal.
- (ix) The transactions are done within delegated powers and wherever exceeded; confirmation /ratification of actions is taken on record.
- (x) That each time a security is acquired it is recorded whether it is for investment or trading account (HFT, HTM, AFS, FVTPL) and, accordingly, accounted in respective accounts based on laid down accounting policies.
- (xi) That investment portfolio is classified into 3 categories of HTM, AFS, FVTPL. The maximum cap of holding under HTM category, i.e., SLR securities holding under HTM is restricted as per latest RBI guidelines.
- (xii) Position regarding holding of securities from other centres where the banks securities are held on behalf of the investment department is to be obtained as of the half year ended September and March.
- (xiii) The statement of securities/stock balance in NDS-OM shall be verified and reconciled with the statements of various securities account, i.e., SGL a/c, CSGl a/c by the concurrent auditors on a daily basis.
- (xiv) Management role of various committees - ALCO, Investment, Trading, Risk Review committee and to monitor their performance.
- (xv) Review of investments, trading activities and reports to ACB/ Board.
- (xvi) Adherence to regulatory guidelines with respect to treasury deals/structured deals. If branch has acted within HO instructions for purchase and sale of securities.

(xvii) Controls around deal modification/ cancellation/ deletion, wherever applicable.

Role of Concurrent Auditor

- Concurrent Auditor Role is also very important in the Investment Management area.
- First the Concurrent Auditor must understand the Investment policy and do the audit.
- Any deviation from the Investment Policy in Investment management, the Auditor must report without any bias.

Repo Transactions

6.6 Banks should follow internal control system and concurrent auditor should ensure that:

- (i) Ready forward transactions are undertaken only against the clear balance of securities in gilt account.
- (ii) All Repo transactions are promptly reported on the NDS and other terms and conditions referred have been complied with.
- (iii) Bank can undertake ready forward transactions only in securities held more than the prescribed SLR requirements.
- (iv) No sale transaction shall be put through in the first leg of ready forward transaction by CSGI constituent without holding the securities in the portfolio.
- (v) Double ready forward deals in any security are strictly prohibited.
- (vi) All repo/ re-repo transactions should be subject to internal audit and concurrent audit. Violation of the regulatory guidelines, if any, may be brought to the notice of Chief General Manager, Financial Markets Regulation Department, Reserve Bank of India, Mumbai.
- (vii) All Repo Rates announced by the RBI must be given effect immediately by the Bank.
- (viii) Concurrent auditor has to see that the Software of the Bank has got the provision to alter/modify the Repo Rate immediately in the system across the India in all its transactions.

Short Sale in Government Securities

- 6.7 Banks may undertake short sale of central government dated securities subject to the short position being covered within a maximum period of three months including the day of trade.

Short sale is defined as a sale of securities one does not own. A bank can also undertake 'notional' short sale, where it can sell a security short from HFT even if the security is held in its AFS/HTM book.

Short sale would include 'notional' short sale. The resultant 'notional' short sale position would be subject to the same regulatory requirements as in the case of a short sale.

Cap on short sale:

Other securities - 1% of the total outstanding stock of each security, or Rs.250 crore, whichever is higher. Liquid securities: 2% of the total outstanding stock of each security, or Rs.500 crore, whichever is higher.

A monthly report of short sale transactions on GOI securities duly certified by the concurrent/internal auditors that there were no violations of extant regulatory guidelines on short sale in G securities be submitted to RBI.

In respect of short sales banks shall ensure adherence to the following:

- (i) The sale leg of the transactions should be executed only on the (Negotiated Dealing System-Order Matching) platform. The cover leg of the short sale transaction can, however, be executed either on or outside the NDS-Om platform.
- (ii) The sale as well as the cover leg of the transaction should be accounted in the HFT- Held for trading category.
- (iii) Short sale transactions shall mark to market daily and account the resultant gains/losses as per the guidelines for marking to market of the HFT portfolio.
- (iv) Under no circumstances, should bank fail to deliver on settlement date, the securities short. Failure to deliver securities short sold shall be treated as an instance of 'SGL bouncing' and bank shall be liable to disciplinary by the RBI.

- (v) Banks has been permitted to use the securities acquired under reverse repo to meet the delivery obligation of the short sale obligation.

Engagement of Brokers

6.8 For engagement of brokers to deal in investment transactions, the banks should observe the following guidelines:

- (i) Transactions between one bank and another bank should not be put through the brokers' accounts.
- (ii) If a deal is put through with the help of a broker, the role of the broker should be restricted to that of bringing the two parties to the deal together.
- (iii) With the approval of their top managements, banks should prepare a panel of approved brokers which should be reviewed annually or more often, if so warranted.
- (iv) Clear-cut criteria should be laid down for empanelment of brokers, including verification of their creditworthiness, market reputation, etc.
- (v) A record of broker-wise details of deals put through and brokerage paid, should be maintained.
- (vi) Banks should fix aggregate contract limits for each of the approved brokers. A limit of 5% of total transactions through brokers (both purchase and sales) entered by a bank during a year should be treated as the aggregate upper contract limit for each of the approved brokers. However, the norm of 5% would not be applicable to banks' dealings through PDs.
- (vii) The concurrent auditors who audit the treasury operations should scrutinize the business done through brokers also and include it in their monthly report.
- (viii) No help of broker is being solicited in inter-bank call money/notice/term money lending and borrowing.

Classification of Investments

1. Classification of investments

- (a) Banks shall classify their entire investment portfolio (except investments in their own subsidiaries, joint ventures and associates) under three categories, viz., Held to Maturity (HTM), Available for Sale (AFS) and Fair Value through Profit and Loss (FVTPL). Held for Trading (HFT) shall be a separate investment sub- category within FVTPL. The category of the investment shall be decided by the bank before or at the time of acquisition and this decision shall be properly documented.
- (b) Banks shall continue to present the investments in the Balance Sheet as set out in The Third Schedule to the BR Act (Form A, Schedule 8 - Investments) as under:
 - (i) Government securities
 - (ii) Other approved securities
 - (iii) Shares
 - (iv) Debentures & Bonds
 - (v) Subsidiaries and / or joint ventures
 - (vi) Others (to be specified)

1.1 HTM

- (a) Securities that fulfil the following conditions shall be classified under HTM:
 - (i) The security is acquired with the intention and objective of holding it to maturity, i.e., the financial assets are held with an objective to collect the contractual cash flows; and
 - (ii) the contractual terms of the security give rise to cash flows that are solely payments of principal⁷ and interest on principal outstanding (*'SPPI criterion'*) on specified dates.
- (b) Notwithstanding the intent with which the following securities are acquired, they shall not meet the SPPI criteria and therefore shall not be eligible for classification either as HTM or AFS:

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- (i) Instruments with compulsorily, optionally or contingently convertible features.
 - (ii) Instruments with contractual loss absorbency features such as those qualifying for Additional Tier 1 and Tier 2 under Basel III Capital Regulations.
 - (iii) Instruments whose coupons are not in the nature of interest **“Interest”** for the purposes of determining eligibility under the solely payments of principal and interest (‘SPPI’) criteria consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin.
 - (iv) Preference shares and Equity shares.
- (c) Investments in the securitization notes, other than the equity tranche, shall be considered to meet the SPPI criteria if the tranche in which the investment is made meets all the following conditions:
- (i) The contractual terms of the tranche being assessed for classification (without looking through to the underlying pool of financial instruments) give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding.
 - (ii) The underlying pool of financial instruments meets the SPPI criteria.
 - (iii) The credit risk of the tranche is equal to or lower than the credit risk of the combined underlying pool of assets.

1.2 AFS

- (a) Securities that meet the following conditions shall be classified under AFS:
- (i) The security is acquired with an objective that is achieved by both collecting contractual cash flows and selling securities; and
 - (ii) the contractual terms of the security meet the ‘SPPI criterion’ as given in HTM para above.

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Provided that on initial recognition, a bank may make an irrevocable election to classify an equity instrument that is not held with the objective of trading (i.e., not held for any of the purposes listed in paragraph 4 of Annex. I) under AFS.

- (b) AFS securities shall *inter-alia* include debt securities held for asset liability management (ALM) purposes that meet the SPPI criterion where the bank's intent is flexible with respect to holding to maturity or selling before maturity.

1.3 FVTPL

- (a) Securities that do not qualify for inclusion in HTM or AFS shall be classified under FVTPL. These shall *inter-alia* include:
 - (i) Equity shares, other than (a) equity shares of subsidiaries, associates or joint ventures and (b) equity shares where, at initial recognition, the irrevocable option to classify at AFS has been exercised.
 - (ii) Investments in Mutual Funds, Alternative Investment Funds, Real Estate Investment Trusts, Infrastructure Investment Trusts, etc.
 - (iii) Investment in securitisation notes which represent the equity tranche of a securitisation transaction. Investments in senior and other subordinate tranches shall need to be reviewed for their compliance with SPPI criterion explained in HTM classification.
 - (iv) Bonds, debentures, etc. where the payment is linked to the movement in a particular index such as an equity index rather than an interest rate benchmark.
 - (v) Securities referred to HTM CLASSIFICATION subject to the exception for equity referred to in sub-clause (i) above.

1.4 HFT

Banks shall create a separate sub-category called HFT within FVTPL. Banks shall comply with the requirements specified in Annex I for classifying investments under HFT.

1.5 Investments in Subsidiaries, Associates and Joint Ventures

All investments in subsidiaries, associates and joint ventures shall be held *sui generis* i.e., in a distinct category for such investments separate from the other investment categories (viz. HTM, AFS and FVTPL).

Measurement of Portfolio

1. HTM

- (a) Securities held in HTM shall be carried at cost and shall not be marked to market (MTM) after initial recognition.
- (b) Any discount or premium on the securities under HTM shall be amortised over the remaining life of the instrument. The amortised amount shall be reflected in the financial statements under item II 'Income on Investments' of Schedule 13.

'Interest Earned' with a contra in Schedule 8: 'Investments'.

2. AFS

- (a) The securities held in AFS shall be fair valued at least on a quarterly basis, if not more frequently. Any discount or premium on the acquisition of debt securities under AFS shall be amortised over the remaining life of the instrument. The amortised amount shall be reflected in the financial statements under item II 'Income on Investments' of Schedule 13: 'Interest Earned' with a contra in Schedule 8: 'Investments'.
- (b) The valuation gains and losses across all performing investments, irrespective of classification (i.e., Government securities, Other approved securities, Bonds and Debentures, etc.), held under AFS shall be aggregated. The net appreciation or depreciation¹¹ shall be directly credited or debited to a reserve named AFS- Reserve without routing through the Profit & Loss Account.
- (c) The AFS-Reserve shall be reckoned as Common Equity Tier (CET) 1 subject to clause 28 of these Directions. The unrealised gains transferred to AFS-Reserve shall not be available for any distribution such as dividend and coupon on Additional Tier 1.
- (d) Upon sale or maturity of a debt instrument in AFS category, the accumulated gain/ loss for that security in the AFS-Reserve shall be

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transferred from the AFS- Reserve and recognized in the Profit and Loss Account under item II *Profit on sale of investments* under Schedule 14-*Other Income*.

- (e) In the case of equity instruments designated under AFS at the time of initial recognition, any gain or loss on sale of such investments shall not be transferred from AFS-Reserve to the Profit and Loss Account. Instead, such gain or loss shall be transferred from AFS-Reserve to the Capital Reserve.

3. FVTPL

- (a) The securities held in FVTPL shall be fair valued and the net gain or loss arising on such valuation shall be directly credited or debited to the Profit and Loss Account. Securities that are classified under the HFT sub-category within FVTPL shall be fair valued on a daily basis, whereas other securities in FVTPL shall be fair valued at least on a quarterly, if not on a more frequent basis.
- (b) Any discount or premium on the acquisition of debt securities under FVTPL shall be amortised over the remaining life of the instrument. The amortised amount shall be reflected in the financial statements under item II 'Income on Investments' of Schedule 13: 'Interest Earned' with a contra in Schedule 8: 'Investments'.

4. Investments in Subsidiaries, Associates and Joint Ventures

- (a) All investments (i.e., including debt and equity) in subsidiaries, associates and joint ventures shall be held at acquisition cost.
- (b) Any discount or premium on the acquisition of debt securities of subsidiaries, associates and joint ventures shall be amortised over the remaining life of the instrument. The amortised amount shall be reflected in the financial statements under item II 'Income on Investments' of Schedule 13: 'Interest Earned'.
- (c) In case where there is already an investment in an entity which is not a subsidiary, associate or joint venture and subsequently the investee entity becomes a subsidiary, associate or joint venture, the revised carrying value as at the date of such investee entity becoming a subsidiary, associate or joint venture shall be determined as under:

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- (i) Where the investment is held under HTM, the carrying value less any permanent impairment shall be the revised carrying value.
 - (ii) Where an investment is held under AFS, the cumulative gains and losses previously recognised in AFS-Reserve shall be reversed and adjusted to the carrying value of the investment along with any permanent diminution in the value of the investment to arrive at the revised carrying value.
 - (iii) Where an investment is held in FVTPL, the fair value as on the date of the investee becoming a subsidiary, associate or joint venture shall be taken as the carrying value.
- (d) When an investee ceases to be a subsidiary, associate or joint venture, the investments shall be reclassified to the respective category¹⁴ as under:
- (i) Where the investment is reclassified into HTM, there shall be no change in the carrying value and consequently no accounting adjustment per se shall be required.
 - (ii) Where the investment is reclassified into AFS or FVTPL, the fair value on the date of such reclassification shall be the revised carrying value. The difference between the revised and previous carrying value shall be transferred to AFS-Reserve and Profit and Loss Account in case of reclassification into AFS and FVTPL respectively.
- (e) Any gain/ profit arising on the reclassification/ sale of an investment in a subsidiary, associate or joint venture shall be first recognised in the Profit and Loss Account and then shall be appropriated below the line from the Profit and Loss Account to the 'Capital Reserve Account'. The amount so appropriated shall be net of taxes and the amount required to be transferred to Statutory Reserves.
- (f) Banks shall evaluate investments in subsidiaries, associates or joint ventures for impairment at least on a quarterly, if not more frequent basis. A non-exhaustive list of indicators of potential impairment is as under:
- (i) The entity has defaulted in repayment of its debt obligations.

- (ii) The loan amount of the entity with any bank has been restructured.
 - (iii) The credit rating of the entity has been downgraded to below investment grade.
 - (iv) The entity has incurred losses for a continuous period of three years and the net worth has consequently reduced by 25 per cent or more.
 - (v) There is a significant decline in the fair value vis-à-vis the carrying value for a period of six months or more. For the purpose of this sub-clause the term significant shall be interpreted as at least 20 per cent. Banks, with the approval of their Boards, may apply even more conservative thresholds.
 - (vi) Any or all the entity's outstanding securities have been delisted, are in the process of being delisted, or are under threat of being delisted from an exchange due to noncompliance with the listing requirements or for financial reasons.
 - (vii) In the case of a new entity/ project where the originally projected date of achieving the breakeven point has been extended i.e., the entity/ project has not achieved break-even within the gestation period as originally envisaged.
- (g) When the need to determine whether impairment has occurred arises in respect of a subsidiary, associate or joint venture, the bank shall obtain a valuation of the investment by an independent registered valuer and make provision for the impairment, if any. Such diminution shall be provided by recognising it as an expense in the Profit and Loss Account. It may be subsequently reversed through Profit and Loss Account, if there is a reversal of the diminution.

Valuation of Investments

Fair Value of Investments

1. The fair value for the purpose of initial recognition and periodical valuation of investments as shall be determined as per the valuation norms laid down as under.
2. **Quoted Securities**

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The fair value for the quoted securities shall be the prices declared by the Financial Benchmarks India Private Ltd. (FBIL) in accordance with RBI circular FMRD.DIRD.7/14.03.025/2017-18 dated March 31, 2018, as amended from time to time. For securities whose prices are not published by FBIL, the fair value of the quoted security shall be based upon quoted price as available from the trades/ quotes on recognised stock exchanges, reporting platforms or trading platforms authorized by RBI/SEBI or prices declared by the Fixed Income Money Market and Derivatives Association of India (FIMMDA).

3. Unquoted SLR Securities

- (a) Treasury Bills shall be valued at carrying cost.
- (b) Unquoted Central / State Government securities shall be valued based on the prices/ YTM rates published by the FBIL.
- (c) Other approved securities shall be valued applying the YTM method by marking them up by 25 basis points above the yields of the Central Government Securities of equivalent maturity put out by FBIL.

4. Unquoted Non-SLR Securities

4.1 Unquoted debentures and bonds:

- (a) Unquoted debentures and bonds shall be valued by applying the appropriate mark-up over the YTM rates for Central Government Securities as put out by FBIL/FIMMDA, subject to the following:
 - (i) The mark-up applied shall be determined based on the ratings assigned to the debentures/ bonds by the credit rating agencies and shall be subject to the following:
 - a. The mark-up shall be at least 50 basis points above the rate applicable to a Central Government security of equivalent maturity for rated debentures/ bonds.
 - b. The mark-up for unrated debentures or bonds shall not be less than the mark-up applicable to rated debentures or bonds of equivalent maturity.

Provided that the mark-up for the unrated debentures or bonds should appropriately reflect the credit risk borne by the bank

- c. Where the debentures/ bonds are quoted and there have been transactions within 15 days prior to the valuation date, the value adopted shall not be higher than the rate at which the transaction has been recorded on the Exchanges/trading platforms/reporting platforms authorized by RBI/ SEBI.
- (b) Ujjwal DISCOM Assurance Yojana (UDAY) bonds and bonds issued by state distribution companies (DISCOMs) under financial restructuring plan:
 - (i) UDAY bonds shall be valued on basis of prices/yields published by FBIL.
 - (ii) State government guaranteed bonds issued and serviced by DISCOM (i.e., when bonds' liabilities are with the DISCOMs) shall be valued by applying a mark-up of 75 basis points on YTM rates for Central Government Securities of equivalent maturities as published by FBIL.
 - (iii) Other bonds issued and serviced by DISCOMs shall be valued by applying a mark-up of 100 basis points on YTM rates for Central Government Securities of equivalent maturities as published by FBIL.
 - (iv) Bonds issued and serviced by the State Government (i.e., when bonds' liabilities are with the State Government) shall be valued by applying a mark-up of 50 basis points on YTM rates for Central Government Securities of equivalent maturities as published by FBIL.
- (c) Special securities, which are directly issued by Government of India, and which do not carry SLR status shall be valued at a spread of 25 basis points above the corresponding yield on Central Government securities of equivalent maturity.
- (d) Zero coupon bonds (ZCBs): In the absence of market value, the ZCBs shall be marked to market with reference to the present value²² of the ZCB. The fair value so determined should be compared with the carrying cost to determine valuation gain or loss.

4.2 Preference Shares

- (a) When a preference share has been traded on exchange within 15 days prior to the valuation date, the value shall not be higher than the price at which the share was traded.
- (b) The valuation of unquoted preference shares shall be done on YTM basis with appropriate mark-up over the YTM rates for Central Government Securities of equivalent maturity put out by the FBIL subject to such preference share not being valued above its redemption value. The mark-up shall be graded according to the ratings assigned to the preference shares by the rating agencies and shall be subject to the following:
 - (i) The mark-up cannot be negative i.e., the YTM rate shall not be lower than the coupon rate/ YTM for a Central Government India security of equivalent maturity.
 - (ii) The rate used for the YTM for unrated preference shares shall not be less than the rate applicable to rated preference shares of equivalent maturity and shall appropriately reflect the credit risk borne by the bank.
 - (iii) Where the investment in preference shares is made as part of a resolution, the mark-up shall not be lower than 1.5 percentage points.
- (c) Where preference dividends/coupons are in arrears, no credit should be taken for accrued dividends/coupons and the value determined as above on YTM basis should be discounted further by at least 15 per cent if arrears are for one year, 25 per cent if arrears are for two years, so on and so forth (i.e., with 10 percent increments). The overarching principle should be that valuation shall be based on conservative assessment of cash flows with appropriate discount rates to reflect the risk. Statutory Auditors should also specifically examine as to whether the valuations adequately reflect the risk associated with such instruments. The depreciation/provision requirement arrived at in respect of non-performing shares where dividends are in arrears shall not be allowed to be set off against appreciation on other performing preference shares.

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- (d) Investments in preference shares as part of the project finance shall be valued at par for a period of two years after commencement of production or five years after subscription whichever is earlier.

4.3 Equity Shares

Equity shares for which current quotations are not available i.e., which are classified as illiquid or which are not listed on a recognised exchange, the fair value for the purposes of these directions shall be the break-up value²³ (without considering 'revaluation reserves', if any) which is to be ascertained from the company's latest audited balance sheet. The date as on which the latest balance sheet is drawn up shall not precede the date of valuation by more than 18 months. In case the latest audited balance sheet is not available or is more than 18 months old, the shares shall be valued at ₹ 1 per company.

4.4 Mutual Funds Units (MF Units)

- (a) Investment in un-quoted MF units shall be valued based on the latest re- purchase price declared by the MF in respect of each scheme.
- (b) In case of funds with a lock-in period or any other Mutual Fund, where repurchase price/ market quote is not available, units shall be valued at Net Asset Value (NAV) of the scheme. If NAV is not available, these shall be valued at cost, till the end of the lock-in period.

4.5 Commercial Paper

Commercial paper shall be valued at the carrying cost.

4.6 Investment in security receipts (SRs) and other instruments issued by an Asset:

Reconstruction Company (ARC)

In respect of investments in SRs and other instruments issued by ARCs, banks shall comply with the requirements of Reserve Bank of India (Transfer of Loan Exposures) Directions, 2021, as amended from time to time.

4.7 Investment in Alternative Investment Funds (AIFs)

- (a) Quoted equity shares, bonds, units of AIFs in the bank's portfolio shall be valued *mutatis mutandis* as per instructions given in these directions for quoted securities.
- (b) Unquoted instruments of AIFs shall be valued as under:

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- (i) *Units*: The valuation shall be done at the NAV as disclosed by the AIF.

Where an AIF fails to carry out and disclose the valuation of its investments by an independent valuer as per the frequency mandated by SEBI (Alternative Investment Fund) Regulations, 2012, the value of its units shall be treated as ₹1 for the purpose of these Directions. In case AIF is not registered under SEBI (Alternative Investment Fund) Regulations, 2012 and the latest disclosed valuation of its investments by an independent valuer precedes the date of valuation by more than 18 months, the value of its units shall be treated as ₹1 for the purpose of these Directions.

- (ii) *Other instruments*: The valuation of unquoted equity and other instruments issued by an AIF shall be as per the methodology specified for such instruments above.

4.8 Conversion of principal and unpaid interest into debt, preference or equity shares In cases of conversion of principal and unpaid interest into debt, preference or equity instruments banks shall follow the requirements of the Prudential Framework for Resolution of Stressed Assets issued vide circular DBR.No.BP.BC.45/21.04.048/2018-19 dated June 7, 2019, as amended from time to time.

Reclassifications between categories

- (i) Banks shall not reclassify investments between categories (viz. HTM, AFS and FVTPL) without the approval of their Board of Directors. Further, reclassification shall also require the prior approval of the Department of Supervision (DoS), RBI.
- (ii) The reclassification should be applied prospectively from reclassification date.
- (iii) When a bank reclassifies investments from one category to another category, the accounting treatment shall be as given in the table below. The bank shall disclose the details of such reclassification including the reclassification adjustments in the notes to the financial statements:

Sl. No.	From	To	Accounting Treatment
a		AFS	The fair value measured at the reclassification date shall be the revised carrying value.

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			Any gain or loss arising from a difference between the revised carrying value and the previous carrying value shall be recognised in AFS-Reserve.
b	HTM	FVTPL	The fair value measured at the reclassification date shall be the revised carrying value Any gain or loss arising from a difference between the revised carrying value and previous carrying value of the investments shall be recognised in the Profit and Loss Account under Item (III): ' <i>Profit on revaluation of investments</i> ' under Schedule 14: ' <i>Other Income</i> '.
c	AFS	HTM	The investments are reclassified at its fair value at the reclassification date. However, the cumulative gain/loss previously recognised in the AFS-Reserve shall be withdrawn therefrom and adjusted against the fair value of the investments at the reclassification date to arrive at the revised carrying value. Thus, the revised carrying value shall be the same as if the bank had classified the investment in HTM <i>ab initio</i> itself.
d		FVTPL	The investments shall continue to be measured at fair value. The cumulative gain or loss previously recognised in AFS- Reserve shall be withdrawn therefrom and recognised in the Profit and Loss Account, under Item (III): ' <i>Profit on revaluation of investments</i> ' under Schedule 14: ' <i>Other Income</i> '.
e		HTM	The carrying amount representing the fair value at the reclassification date remains unchanged.
f	FVTPL	AFS	

Non-Performing Investments (NPI)

- (a) The criterion used to classify an asset as Non-Performing Asset (NPA) as per the extant Prudential Norms on Income Recognition, Asset Classification and Provisioning (IRACP) pertaining to Advances shall be used to classify an investment as a Non-Performing Investment (NPI). Similarly, an NPI shall only be upgraded to standard when it meets the criteria specified in the IRACP norms.
 - (i) In respect of debt instruments such as bonds or debentures, an NPI is one where interest/ instalment (including maturity proceeds) is due and remains unpaid for more than 90 days.
 - (ii) Sub-clause (a)(i) above shall apply, mutatis mutandis to preference shares where the fixed dividend is not paid. If the dividend on preference shares (cumulative or non-cumulative) is not declared / paid in any year it shall be treated as due / unpaid in arrears and the date of balance sheet of the issuer for that particular year shall be reckoned as due date for the purpose of asset classification. Such an investment can be upgraded subsequently on payment of dividend for the current period in the case of non-cumulative preference shares and payment of dividend in arrears and for current period in the case of cumulative preferences shares.
 - (iii) In the case of equity shares, in the event the investment in the shares of any company is valued at ₹1 per company on account of the non-availability of the latest balance sheet, equity shares shall be reckoned as NPI. The NPI can be upgraded subsequently on receipt of audited balance sheet.
 - (iv) If any credit facility availed by the issuer is NPA in the books of the bank, investment in any of the securities, including preference shares issued by the same issuer shall also be treated as NPI and vice versa. However, this stipulation shall not be applicable in cases where only the preference shares are classified as NPI, and in such cases, the investment in any of the other performing securities issued by the same issuer need not be classified as NPI and any performing credit facilities granted to that borrower need not be treated as NPA.

- (v) In case of conversion of principal and / or interest into equity, debentures, bonds, etc., such instruments shall be categorised in HTM, AFS or FVTPL (including HFT) at the time of initial recognition, as per the requirements of Chapter III above. Further, the asset classification of such instruments shall be same as the loan and provision shall be made as per the norms.
- (b) Once an investment is classified as an NPI, it should be segregated from rest of the portfolio and not considered for netting valuation gains and losses.
- (c) Banks shall not accrue any income on NPIs. Income shall be recognised only on realisation of the same. Further, any MTM appreciation in the security shall be ignored.
- (d) Irrespective of the category (i.e., HTM, AFS or FVTPL (including HFT)) in which the investment has been placed, the expense for the provision for impairment shall always be recognised in the Profit and Loss Account. The provision to be held on an NPI shall be the higher of the following amounts:
 - (i) The amount of provision required as per IRACP norms computed on the carrying value of the investment immediately before it was classified as NPI; and
 - (ii) The depreciation on the investment with reference to its carrying value on the date of classification as NPI.

In view of the above, no additional provision for depreciation shall be required over and above the provision for NPI as specified above.

Provided that in the case of an investment categorised under AFS against which there are cumulative gains in AFS-Reserve, the provision required may be created by charging the same to AFS-Reserve to the extent of such available gains.

Provided further that in the case of an investment categorised under AFS against which there are cumulative losses in AFS-Reserve, the cumulative losses shall be transferred from AFS-Reserve to the Profit and Loss Account.

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- (e) Upon an account being upgraded as per IRACP norms, any provision previously recognised shall be reversed and symmetric recognition of MTM gains and losses can resume.
- (f) Investments in Government securities and Government guaranteed investment:
 - (i) Investments in Central Government Securities and State Government Securities shall not be classified as NPI.
 - (ii) Investments in Central Government guaranteed securities shall also not be classified as NPI until the Central Government has repudiated the guarantee when invoked. In respect of such securities held in AFS and FVTPL, banks shall continue to recognise MTM gains/losses in AFS-Reserve and Profit and Loss respectively. However, any income shall be recognised only on realisation basis.
 - (iii) Investment in State Government guaranteed securities, shall attract prudential norms for identification of NPI and provisioning, when interest/ instalment of principal (including maturity proceeds) or any other amount due to the bank remains unpaid for more than 90 days.

Hardware and Software

6.9 Following are some important points related to hardware and software:

- (i) All necessary systems – computer, servers, printers, telephone, fax, internet connections – RTGS, NDS, wire agency connections (as per regulatory prescriptions).
- (ii) Physical layout of the dealing room, mid and back-office connectivity, stock flow.
- (iii) Regulatory connectivity – CCIL, RBI, DAD, PDO connectivity, etc.
- (iv) Stock maintenance software, deal market generation, reconciliation, voice recording, etc.
- (v) Programs to run the systems as necessary.
- (vi) Package to run Var and other risk measurement tools.

Maintenance of Cash Reserve Ratio by the Bank

6.10 The auditors are required to check and certify that:

- (i) Department which computes demand and time liabilities of bank has computed the obligatory CRR for the fortnight correctly and informs funds management department timely for maintenance of CRR.
- (ii) There is no default in maintenance of CRR and in case of default whether it has been reported to top management or board.
- (iii) Detailed Guidelines for System of compiling Net Demand and Time Liabilities (NDTL) position are given in RBI Master Circular RBI/2015-16/98.

The following RBI Circulars must be read by the Concurrent auditor before taking any decision.

- (a) DBR.No. Ret.BC.24/12.01.001/2015-16 "Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR)" dated July 1, 2015.
- (b) Master Directions: RBI/DOR/2021-22/80 DOR NO. RET.REC.32/12.01.001/2021-22 dt 20.07.2021.
- (c) RBI/2022-23/150 DOR.MRG.REC.89/21.04.141/2022-23/dt 8.12.2022.

Maintenance of Statutory Liquidity Ratio by the Bank

6.11 The auditors are required to check and certify that:

- (i) The bank had correctly computed DTL/NDTL and has maintained required SLR on daily bases and no default has taken place during the period. In case of any default, the same is reported to appropriate authority with amount of penalty paid to RBI.
- (ii) Bank is submitting to the RBI before 20th day every month a return in Form VIII showing the amounts of SLR held on alternate Fridays during immediately preceding month with particulars of their DTL.
- (iii) Bank is also submitting a statement as annexure to form VIII giving daily position of (a) value of securities held for the purpose of compliance with SLR and (b) the excess cash balance maintained by them with RBI in the prescribed format.
- (iv) System of compiling Net Demand and Time Liabilities (NDTL) position.

Borrowings and Lending in Inter-Bank Call Money Market

6.12 The auditors are required to check and certify that following prudential limits for transactions in call/ notice money market as specified by the RBI have been adhered to:

Table 1: Prudential limits for outstanding borrowing transactions in Call, Notice and Term Money Markets		
Sr. No.	Participant Category	Prudential Limit
1	<u>Scheduled Commercial Banks</u> ¹	Call, Notice and Term Money: Internal board approved limits within the prudential limits for inter-bank liabilities prescribed by Department of Regulation.
2	Small Finance Banks	Call and Notice Money: (i) 100% of capital funds, on a daily average basis in a reporting fortnight, and (ii) 125% of capital funds on any given day. Term Money: (i) Internal board approved limit within the prudential limits for inter-bank liabilities.
3	Payment Banks, and Regional Rural Banks	Call, Notice and Term Money: (i) 100% of capital funds, on a daily average basis in a reporting fortnight, and (ii) 125% of capital funds on any given day.
4	Co-operative Banks	Call, Notice and Term Money: (i) 2.0% of aggregate deposits as at the end of the previous financial year.
5	Primary Dealers	Call and Notice Money: (i) 225% of Net Owned Fund (NOF) as at the end of the previous financial year on a daily average basis in a reporting fortnight. Term Money²: (i) 225% of Net Owned Fund (NOF) as at the end of previous financial year.

Asset Liability Management and Risk Management

6.13 The auditor is expected to make comment on the following aspects:

- (i) Existence of Policy on Asset – Liability Management and monitoring thereof; compliance with the RBI guidelines.
- (ii) Review of MCLR- from 1.4.2016 (marginal cost of fund-based lending rate) once in a month.
- (iii) Risk Management Policy – approach, tools (Var, PVBP) limits, measurement, monitoring and follow-up. Stop Loss Policy should be approved by the Board. Sanctioning Authority for Security Transactions.

6.14 The auditor should check:

- (i) That all transactions in securities are having sanction strictly in accordance with the limits laid down in bank's investment policy.
- (ii) That the total exposure in one group of companies is indicated and considered while making the investment and these facts are clearly mentioned in the office memorandum seeking sanction from the higher authorities.
- (iii) The Repo/Reverse Repo transactions undertaken by the bank under liquidity adjustment facility with RBI through auction process are as per the rules prescribed by the RBI.

Reporting/ Review Systems for Security Transaction

6.15 The auditor should verify that:

- (i) Daily reports on funds and investment position are put up to top management.
- (ii) Monthly sale/ purchase transactions are reported to the Board.
- (iii) Balances as per bank's books are reconciled with the balances in the books of public debt office of RBI.
- (iv) All office memoranda for transactions confirmed/sanctioned are serially numbered and are recorded in the register maintained by the bank.
- (v) In every Board meeting, a report on funds and treasury management including derivatives giving the position as on the last reporting Friday of every month from the previous Board meeting is placed.

- (vi) Checking of application money, reconciliation of SGL account, compliance to RBI norms should be done.

Investments in Privately Placed Instruments

6.16 The auditor should verify that:

- (i) The issuer should issue an offer document with terms of issue, authorized by Board resolution.
- (ii) Bank shall stipulate entry level ratings, quality standards and industry wise, maturity wise, duration wise, issuer wise limits to mitigate the adverse impacts of concentration and the risk of liquidity.
- (iii) Bank shall undertake usual due diligence analysis before making investments in Non SLR securities.

Record Keeping, Monitoring, Reporting, MIS & Statements

6.17 The auditors are required to check and certify that:

- (i) There is functional segregation of dealing, settlement and accounting in funds management.
- (ii) There exist proper recordkeeping and reporting backed by strong MIS.
- (iii) Review of funds position is periodically done, and top management is informed about the positions on daily basis.
- (iv) Reviews required by the board are placed within the time frame.
- (v) Exposure limits for inter-bank lending with counterparty are reviewed annually and limits fixed.
- (vi) RBI's guidelines for valuation of securities for the purpose of SLR is being followed.
- (vii) Top management is informed on interest in arrears, securities matured but amount not received and on the system of follow up for each of these.
- (viii) All returns required to be submitted to internal and external agencies have been prepared correctly and submitted timely.

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- (ix) There is harmonious co-operation and exchange of information between investment department/MIS department and credit department.
- (x) Checking of custody of unused BR Forms.
- (xi) Use of Bank Receipt (BR).

Derivatives

6.18 The auditors are required to check and certify that:

- (i) Board has approved derivate trading policy.
- (ii) In case of derivate transactions with clients, treasury will follow. Suitability and appropriateness policy for derivatives guidelines issued by the RBI and FIMMDA.
- (iii) Periodic confirmation of Derivative contracts with counterparties.
- (iv) Cancellation of forward contracts and passing/recovery of exchange gain/loss.
- (v) Gaps and Open position Limit (OPL) maintained in different currencies vis-à-vis prescribed limit for the same. Aggregate Gap limit (AGL) of the Bank is approved by RBI after bank's Board Recommendation. AGL should not exceed 6 times of total capital (Tier I & Tier II) of the bank. Net Open Overnight Position (NOOPL) of the bank should not exceed 25% of total capital (Tier I & Tier II) of the bank.
- (vi) Reconciliation of Nostro and Vostro accounts balances in Nostro accounts in different foreign currencies are within the limits prescribed by the bank.
- (vii) Collection of underlying documents for derivative and forward contracts. Delays, if any.
- (viii) Instances of booking and cancellation of forward contracts with the same counterparty within a span of couple of days or a few days.
- (ix) Sample check some of the deals and comments on the correctness of computation.

Disclosure Norms

6.19 The disclosure norms as set out by the RBI should be followed scrupulously. Disclosures are to be made strictly as per the RBI

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prescribed format and the same are to be got certified by statutory auditors. RBI "RBI/DOR/2021-22/83DOR.ACC.REC. No.45/21.04.018/2021-22 August 30, 2021 is important for this purpose.

Compliance

6.20 Following are important aspects with respect to Compliance:

- (i) To ensure that the treasury operations of the bank have been conducted in accordance with the instructions issued by the RBI, SEBI from time to time.
- (ii) Compliance officer to ensure compliance to regulation and internal guidelines.
- (iii) Ensuring compliance to other regulators and correspondence with regulators.
- (iv) Sustenance of compliance to various audit observations.

Special-Purpose Certificates Relating to Investments

6.21 Banks require their central auditors to issue the following certificates regarding investments of the bank, in addition to their main audit report and the long form audit report:

- (i) Certificate on reconciliation of securities by the bank (both on its own Investment Account as well as PMS clients' account).
- (ii) Certificate on compliance by the bank in key areas of prudential and other guidelines relating to such transactions issued by the Reserve Bank of India. Master Direction - Classification, Valuation and Operation of Investment Portfolio of Commercial Banks (Directions), 2023 RBI/DOR/2023-24/104 DOR.MRG.36/21.04.141/2023-24 September 12, 2023 (Updated as on April 01, 2025) must be adhered to.

Annexure I

Illustrative List of Reports Placed before the Board/ Audit Committee of the Board (ACB) regarding Treasury Function

1	Sale / Purchase of transactions	Board	Monthly
2	Report on Funds Management/Achievement of investment policy objectives.	Board	Monthly
3	Reconciliation of Govt securities (PDO A/c.) with RBI	ACB	Monthly
4	Transactions in equity shares/convertible bonds and debentures/ equity oriented Mutual Funds	ACB	Monthly
5	Capital Market Exposure	ACB	Monthly
6	Report of short sale transactions in GOI securities	Board	Monthly
7	Brokers Exposure Limit	Board	Quarterly
8	Overdue position of SLR/Non-SLR investments	Board	Quarterly
9	Review of non-SLR investments	Board	Quarterly
10	Information in respect of equity shareholding in borrower companies	ACB	quarterly
11	Review of bank's funds position/statutory requirements and investment portfolio	Board	Half Yearly
12	Review of panel of brokers	Board	Annually
13	Review of investment policy	Board	Annually
14	Transactions with related parties during the financial year	ACB	Annual

Annexure II
Abbreviations

ACB	Audit Committee of the Board
AFS	Available for Sale
CBLO	Collateralized Borrowing and Lending Obligation
CCIL	Clearing Corporation of India Limited
CSGL	Constituent Subsidiary General Ledger
CRR	Cash Reserve Ratio
DVP	Delivery verses Payment Systems
FIMMDA	Fixed Income Money Market and Derivatives Association of India
HFT	Held for Trading
HTM	Held to Maturity
MCLR	Marginal Cost of Fund Based Lending Rate
MTM	Marked to Market
NDS	Negotiated Dealing system
NDS-OM	Negotiated dealing system- Order Matching
NDTL	Net Demand and Time Liabilities
PDAI	Primary Dealers Association of India
PDO	Public Debt Office
REPO	Repurchase Obligation
SGL	Subsidiary General Ledger
SLR	Statutory Liquidity Ratio
STRIPS	Separate Trading of Registered Interest and Principal Securities
RTGS	Real Time Gross Settlement Systems
VAR	Value at Risk

Chapter 7

Foreign Exchange

- 7.1 All foreign exchange transactions in India are conducted under Foreign Exchange Management Act, 1999 (FEMA) (here in after referred to as “the Act”) effective from 1.6.2000 repealing the Foreign Exchange Regulation Act, 1973 (FERA) which was in force since 1.1.1974. FEMA contains 49 sections.
- 7.2 All forex transactions conducted can broadly be bifurcated into:
- A. Current Account Transactions and
 - B. Capital Account Transactions.
- (a) Current account transactions are regular and recurring in nature, viz.,
 - (i) Export remittances,
 - (ii) Import remittances,
 - (iii) NRI remittances, etc., and
 - (iv) Rupee is fully convertible on current account transactions.
 - (b) Capital account transactions are those transactions which results in creation of an asset or a liability for a resident overseas or for a non-resident in India.
 - (c) Capital account alters the assets/liabilities position in the balance sheet of the Indian entity.
 - (d) All current account transactions are free unless restrictions are imposed by Central Government under Section 3 of FEMA.
 - (e) In respect of Current Account transactions, rules are made by Government of India under Section 46 of the Act (five rules have been made so far).
 - (f) Capital account transactions are permitted unless restricted or imposed by Reserve Bank of India vide Section 6 of the Act.
 - (g) In respect of Capital Account transactions, regulations are made by Reserve Bank of India under Section 47 of the Act and 23 regulations have been made so far.

- (h) RBI has been authorized to control Foreign Exchange transactions in India and the same is clearly mentioned in Section 10 of FEMA 1999.
- (i) RBI will not involve directly into any Foreign Exchange transactions and the same is carried out by the Authorised Persons (who are also called as Authorised Dealers) as per the Directions of RBI.
- (j) In addition to these guidelines, Reserve Bank of India and Government of India, periodically, release notifications to effect changes in Capital and Current account transaction, respectively.
- (k) The concept of issuing master circulars on 1st week of July every year is now dispensed with and instead Master directions are issued by Reserve Bank of India.
- (l) Master Directions are issued every year on the first of January consolidating the instructions issued till date and, they are updated as and when changes are made through notifications and / or directions.

Note: Master Directions (consolidated) are issued regularly on every 1st January of Every Year and the same is updated as and when required (Please Ref: www.rbi.org.in)

Besides the above Master Directions, the following Master Circulars issued by the Reserve Bank of India are also relevant for understanding the subject of foreign exchange (with regular updates).

- (i) Foreign Investments in India.
- (ii) Money Transfer Service Scheme.
- (iii) Risk Management and Interbank dealings.
- (iv) Rupee / FC Export credit and customer service to exporters.

Important Definition to Understand the Subject Foreign Exchange

7.3 The following definitions are relevant for understanding the subject of Foreign Exchange:

(a) Foreign Exchange:

Foreign Exchange means foreign currency, and includes:

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- 1) All deposits, credits and balances payable in foreign currency, and any drafts, traveller's cheques, letters of credit and bills of exchange, expressed or drawn in Indian currency and payable in foreign currency.
- 2) Any instrument payable at the option of the drawer or holder, thereof or any other party thereto, either in Indian currency or in foreign currency, or partly in one and partly in the other. Debit cards, ATM cards or any other instrument which can be used to create a financial liability may be defined as currency.

(Section 2 (n) of FEMA, 1999)

(b) Capital Account Transaction:

The following transactions conducted by Person resident in India are treated as Capital Account Transactions as per Schedule I (Regulation 3(1) A of the Act):

- (i) Investments in foreign securities.
- (ii) Foreign currency loans raised in India and abroad.
- (iii) Transfer of immovable property outside India.
- (iv) Guarantees issued in favour of a person resident outside India.
- (v) Export, import and holding of currency / currency notes.
- (vi) Loans and Overdrafts (borrowings) from a person resident outside India.
- (vii) Maintenance of foreign currency account in India and outside India.
- (viii) Taking out of Insurance policy from an insurance company outside India.
- (ix) Loans and overdrafts given to a person resident outside India.
- (x) Remittance outside India of capital assets.
- (xi) Sale and purchase of foreign exchange derivatives in India and abroad and commodity derivatives abroad.

The following transactions conducted by Person resident in India are treated as Capital Account Transactions as per Schedule II (Regulation 3(1) A of the Act):

- (A) Investments in India:
- issue of security by a body corporate or an entity in India and investment therein.
 - investment by way of contribution to the capital of a firm or a proprietorship concern or an association of persons in India.
- (B) Acquisition and transfer of immovable property in India.
- (C) Guarantee issued in favour of or on behalf of, a person resident in India.
- (D) Import and export of currency notes into/from India.
- (E) Deposits between a person resident in India and outside India.
- (F) Foreign currency account in India.
- (G) Remittance outside India of capital assets in India of a person resident outside India.

(c) Current Account Transaction:

Current Account Transaction means a transaction other than capital account transaction, but includes the following (section 2(j) of FEMA):

- (a) Payment due in connection with foreign trade, other current business, services and short-term banking and credit facilities in the ordinary course of business.
- (b) Payments due as interest on loans and as net income from investments.
- (c) Remittances for living expenses of parents, spouse and children residing abroad, and
- (d) Expenses in connection with foreign travel, education and medical care of parents, spouse and children.

(d) Authorised Person:

Section 2(c) of the Act, states that “authorised person” means an authorised dealer, money changer, offshore banking unit or any other person authorised under section 10 (1) to deal in foreign exchange and foreign securities. These are authorised by Reserve Bank of India under Section 10 of FEMA to deal in foreign exchange. They are broadly classified as under:

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AD CATEGORY I	COMMERCIAL BANKS STATE COOP BANKS URBAN CO OP BANKS	All current and capital account transactions
AD CATEGORY II	UPGRADED FFMCS COOP BANKS RRBS	Non-trade related current account transactions specified by Reserve Bank and all activities permitted for FPMC.
AD CATEGORY III	SELECT FINANCIAL AND OTHER INSTITUTIONS	Transactions incidental to the foreign exchange undertaken by them
FPMC (FULL FLEDGED MONEY CHANGERS)	DEPT OF POSTS URBAN COOP BANKS OTHER FFMCS	Purchase and sale of foreign exchange for private and business visits abroad.

Category of Branches

The Authorized Dealers (Banks) who have huge network of branches bifurcate their branches into Three Category viz Category A, B and C branches. These branches are allowed to transact in various activities permitted under FEMA. Mostly the assignments will be as under:

(i) CATEGORY A BRANCHES

- Maintains Foreign Currency Accounts in banks abroad and maintains foreign exchange positions.
- Buy / sell foreign currencies in the interbank forex market.
- Provide cover to branches for the forex transactions of their clients.
- Provide forward cover to merchants through their Branches.
- Compliance to RBI / GOI guidelines.
- Provide buying and selling rates to branches.
- Balancing of Nostro Accounts.

The dealing room of the Bank, the Trade Finance Centre of the Bank are the A category Branches.

(ii) CATEGORY B BRANCHES

- Operate foreign currency accounts maintained by category A branches with foreign banks abroad.
- Issue remittances/ demand drafts drawn in foreign currency and encase for customers.
- Handle exports and import business for the clients.
- Handle all remittance transactions both and current account and capital account transactions.
- Maintain deposit accounts of NRIs such as FCNR, NRE, NRO, EEFC, Diamond Dollar Account, etc.

The B category branches are identified through the AD code (Authorized Dealers Code) issued by the RBI for conducting the foreign exchange business for the customers.

(iii) CATEGORY C BRANCHES

Normally, they are not allowed to conduct any foreign exchange transactions on their own and route through category B branches. C Category Branches are allowed to open FCNR, NRE, NRO, RFC, EEFC and special foreign currency accounts for their customers.

(e) Person includes (i) individual, (ii) a Hindu Undivided family, (iii) a company, (iv) a firm, (v) an association of persons or a body of individuals whether incorporated or not, (vi) every artificial judicial person, not falling in any of the preceding sub-clauses, and (vii) any agency, office, or branch owned or controlled by such person.

(f) Person Resident in India means:

- (i) a person residing in India for more than 182 days during the course of the preceding financial year, but does not include, a person who has gone out of India or who stays outside India, in either case –(A) (a) for or on taking up employment outside India, or (b) for carrying on outside India a business or vocation outside India or (c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period. (B) A person who has come to stay in

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India, in either case, or otherwise than –(a) for or on taking up employment in India, or(b) for carrying on in India a business or vocation in India or (c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period.

- (ii) any person or body corporate registered or incorporated in India.
- (iii) an office, branch or agency in India owned or controlled by a person resident outside India.
- (iv) an office, branch or agency outside India owned or controlled by a person resident in India. (Section 2 (v) of the Act).

(g) Person resident outside India means a person who is not resident in India. The definition of Non-resident and Person of Indian Origin (PIO) have been defined differently in various guidelines and hence should be guided in that context only.

Similarly, the definition of “relative” should be referred to the context as it has been defined under section 6 of Companies Act, 1956 and Companies Act, 2013, separately.

Current Account Transactions

7.4 Persons resident in India can undertake various current account transactions as per rules framed there under. The detailed rules issued by Government of India are as under:

S.no.	Rule	Details
1	Foreign Exchange Management (Encashment of Draft, Cheque, instrument and payment of interest) Rules, 2000	Deals with these instruments to be delivered to investigating agencies where investigation was referred under section 37 of the Act.
2	Foreign Exchange Management (Authentication of Documents) Rules, 2000	Notifying that the documents received in India and signed by Diplomatic and Consular Officers is treated as notarized.

Foreign Exchange

3	Foreign Exchange Management (Current Account Transactions) Rules, 2000 effective 1.6.2000	Deals with various current account transactions, prohibited, restricted, and permitted to persons.
4	Foreign Exchange Management (Adjudication Proceedings and appeal) Rules, 2000	Appointment of Adjudicating authorities for holding inquiry.
5.	Foreign Exchange (compounding proceedings) Rules 2000	Powers of Reserve Bank of India to compound contravention.

7.5 Current Account transactions are permitted under Foreign Exchange Management (Current Account Transactions) Rules, 2000 effective 1.6.2000 (updated from time to time) can be broadly classified into three schedules. Schedule I transaction are strictly prohibited; Schedule II transactions require prior approval of the Central Government and Schedule III transactions are permitted by Authorised dealers within the limits stipulated against each transaction.

(i) Schedule I transactions

The following transactions are prohibited as per Schedule I:

- (i) Remittance out of lottery winnings.
- (ii) Remittance of income from racing/riding, etc., or any other hobby.
- (iii) Remittance for purchase of lottery tickets, banned/prescribed magazines, football pools, sweepstakes, etc.
- (iv) Payment of commission on exports made towards equity investment in Joint Ventures/Wholly Owned Subsidiaries abroad of Indian companies.
- (v) Remittance of dividend by any company to which the requirement of dividend balancing is applicable.
- (vi) Payment of commission on exports under Rupee State Credit Route, except commission up to 10% of invoice value of exports of tea and tobacco.
- (vii) Payment related to "Call Back Services" of telephones.

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(viii) Remittance of interest income on funds held in Non-resident Special Rupee Scheme account.

In addition to the above, drawl of foreign exchange is prohibited for travel to Nepal and / or Bhutan and a transaction with a person resident in Nepal or Bhutan without Reserve Bank of India approval.

(ii) Schedule II transactions

The following Schedule II transactions require prior approval of Central Government of India:

S. No.	Purpose of remittance	Department to approve.
1	Cultural Tours	Ministry of Human Resources Development, (Department of Education and Culture)
2	Advertisement in foreign print media for purposes other than promotion of tourism, foreign investments and international bidding (exceeding USD 10,000) by a State Government and its Public Sector Undertakings	Ministry of Finance, (Department of Economic Affairs)
3	Remittance of freight chartered by a PSU of vessel	Ministry of Surface Transport, (Chartering Wing)
4	Payment of import by a Govt. Department or a PSU on c.i.f. basis (i.e., other than f.o.b. and f.a.s. basis)	Ministry Transport, of Surface (Chartering Wing)
5	Multi-modal transport operators making remittances to their agents abroad	Registration Certificate from the Director General of Shipping
6	Remittance of hiring charges of transponders by (a) TV channels (b) internet service providers	Ministry of Information and Broadcasting Ministry of Communication and IT

Foreign Exchange

7	Remittance of container detention charges exceeding the rate prescribed by Director General of Shipping	Ministry of Surface Transport (Director General of Shipping)
8	Remittance of Prize Money / sponsorship of sports activity abroad by a person other than Sports bodies if the amount involved exceeds USD 100000	Ministry of HR
9	Remittance for membership of P & I club Insurance	Ministry of Finance

(iii) Schedule III transactions

The following Schedule III transactions are affected by the Authorized Dealers, up to the limits specified thereof, and all transactions exceeding the limits mentioned therein requires Reserve Bank of India prior approval:

- (i) Release of exchange in one financial year for one or more private visits to any country except Nepal and Bhutan.
- (ii) Gift remittance for financial year per remitter or donor other than resident individual.
- (iii) Donation per financial year per remitter or donor other than resident individual.
- (iv) Exchange facilities for persons going abroad for employment.
- (v) Exchange facilities for emigration or amount prescribed by country of emigration whichever is lower.
- (vi) Remittance for maintenance of close relatives abroad, exceeding net salary (after deduction of taxes, contribution to provident fund and other deductions) of a person who is resident but not permanently resident in India and:
 - (a) is a citizen of a foreign State other than Pakistan; or
 - (b) is a citizen of India, who is on deputation to the office or branch or subsidiary or joint venture in India of such foreign company.
 - (c) exceeding US\$1,00,000 per year per recipient, in all other cases.

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Explanation: For this purpose, a person resident in India on account of his employment deputation of a specified duration (irrespective of length thereof) or for a specific job or assignment, the duration of which does not exceed three years, is a resident but not permanently resident].

- (vii) Release of foreign exchange to a person, irrespective of stay, for business travel, or attending a conference or specialized training or for maintenance of expenses of a patient going abroad for medical treatment or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment or check-up.
- (viii) Release of foreign exchange for meeting expenses for medical treatment abroad as per the estimate from the doctor in India or hospital / doctor abroad.
- (ix) Release of foreign exchange for studies abroad or up to the estimates given by the institution abroad.

Liberalized Remittance Scheme (LRS)

- (i) The scheme was introduced on February 4, 2004, vide A.P. (DIR Series) Circular No. 64 dated February 4, 2004, read with Go Notification G.S.R. No.207(E) dated March 23, 2004, as a liberalization measure to facilitate resident individuals to remit funds abroad for permitted current or capital account transactions or combination of both.
- (ii) These guidelines are modified from time to time.
- (iii) As per the scheme, all the above remittances allowed to individuals (only individuals including Minor) are subsumed under this scheme.
- (iv) As per the present guidelines, a person can remit up to USD 250,000 per financial year to one of those transactions or a combination thereof total not exceeding USD 250,000 (or its equivalent) per Financial Year/ per account.
- (v) In case there is a Joint account in the name of the Two individual (e.g. mother and son), the limit is applicable for single transfer and not individually for both (mother and son). That means from one account under LRS one can transfer only USD 250000 or its equivalent. (Example):
 - If mother transfers USD 250000 from the account and the son can transfer USD "0" only.

Foreign Exchange

- If mother transfers USD 100000 from the account, the son can transfer only up to USD 150000.
- If mother wants to transfer USD 250000 and son wants to transfer USD 250000, under LRS only USD 250000 is allowed to be transferred and not entire USD 500000.

(vi) The Scheme is not available to the following entities:

- Corporates
- Partnership Firms
- HUF
- Trusts
- Transactions not permissible under FEMA

In addition to the above facilities available for remittance to individual persons, the Authorized Dealer is also permitted to make remittances to other than individuals as under. These are not covered under LRS:

Foreign Exchange

1.	Commission, per transaction to agents abroad (for sale of residential flats or commercial plots in India)	25,000 or 5 % of Inward remittance whichever is more
2.	Consultancy services procured from outside India per project. Infrastructure project	1,000,000 10,000,000
3.	Reimbursement of pre-incorporation expenses Remittances exceeding 5% of investment brought into India or USD 100000 whichever is higher.	100,000
4.	Advertisement Abroad in Media outside India Insurance premium for Health insurance from foreign company. Subscription to magazines. If web services are for the business of the company International Credit Cards.	Fully allowed subject to satisfaction of the Authorized Dealer

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5.	Donations not exceeding 1% of foreign exchange earnings during the previous three financial years or USD 5 MN whichever is less for: <ul style="list-style-type: none">• Creation of chairs in reputed educational Institutes.• Contributions to funds promoted by educational institutes and• Contribution to technical institution of the donor company.	USD 5 Million
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However, there are no restrictions as to quantum of amount of remittance in respect of the following transaction, subject to that the transaction is to the satisfaction of the authorized dealer, and is as per the guidelines issued by Government of India/ Reserve Bank of India from time to time:

- (i) Payments for import of goods.
- (ii) Remittance of interest on investment made from abroad.
- (iii) Remittance of interest on funds borrowed from abroad.
- (iv) Remittance of dividend.
- (v) Booking of passage for foreign travel with airline/ shipping companies or booking of cargo in ships/ aircrafts. Indian office can accept payment in rupees and make payment in foreign currency.
- (vi) Remittances from RFC/ EEFC accounts.
- (vii) Export Commission.
- (viii) Remittance can be made for payment towards advertisement in print or internet or TV abroad.
- (ix) Payment to EOU/ SEZ by units in DTA. An EOU/ SEZ may supply goods in units in DTA and DTA can make payment in FC to them which will be credited to FC accounts of SEZ and EEFC of other units.

All the above are subject to deduction of tax at source and other regulations for respective schemes.

Notes:

- 1. Under LRS any individual can transfer the funds to the extent of USD 250000 or its equivalent without RBI permission.

2. With RBI permission anybody can transfer any amount of USD or in foreign currency to anyone.
3. The remitter is required to submit Form A-2 to the Authorized Dealer before making any remittance for the above purposes, if the remittance is above USD 25,000 and only a simple declaration form for all the remittances up to USD 25,000 (as per individual Bank's guidelines).

The remittances may also attract provision under section 195 (6) Income Tax Act, 1961, which requires the person paying to NRI to furnish the information. As per Rule 37 BB information should be submitted to Income Tax if paying to a non-resident, not being a company or to a foreign company in Form 15 CA and Form 15 CB.

4. It is pertinent to note that FEMA guidelines clearly mention that payment of taxes/ duties/ levies and or any other payments due to any government departments are subject to the individual guidelines issued by the respective departments and constituents availing forex facilities need to abide by those guidelines.

Liberalized Remittance Scheme applicable to Individuals

7.6 The general guidelines are as under:

- Remittances by Resident Individuals up to USD 250,000 or its equivalent per Financial Year/per account for any permitted current or capital account transaction or combination of both.
- The scheme is not available to corporate, partnership firms, HUF, Trusts, etc.
- In case of minor, minor's natural guardian will sign the declaration form.
- Remittances can be consolidated in respect of family members.
- Clubbing is not permitted for capital account transactions such as bank accounts, investment, purchase of property if they are not co-owners/co-partners.
- A resident cannot gift to another resident in foreign currency for the credit of latter's Foreign Currency account abroad under LRS.
- The customer must maintain account with the Bank for a minimum period of one year prior to remittances of capital account transactions.

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- Banks should not give any credit facility to resident individuals to facilitate capital account remittances.
- PAN card is mandatory Up to USD 25,000 PAN need not be insisted upon.
- Resident must designate a specific bank to route all transactions under LRS.
- Resident must maintain account for a period of one year.
- New customers should produce statement of account of previous bank.

A declaration in the specified format should be submitted to the bank. Form A-2 to be filled in. A simple declaration may be obtained up to USD 25000.

7.7 The following capital account transactions are permitted under LRS:

- (a) Opening of accounts abroad with a bank.
- (b) Purchase of property.
- (c) Investment in shares, mutual funds, venture capital funds, unrated debt securities and promissory.
- (d) Set up wholly owned subsidiaries and joint ventures.
- (e) Extending loans (FC and Rupee both) to Non-Resident Indians who are relatives as defined in Companies Act, 1956.

7.8 The following current account transactions are permitted:

- (a) Includes those listed in Schedule III.
- (b) May allow as Gift to a person residing outside India or as donation to an organization outside India.
- (c) Maintenance of close relative as defined in Companies Act, 1956.
- (d) Objects of art can be purchased.
- (e) Outward remittance can be allowed in the form of DD either in the name of resident individual or in the name of the beneficiary with whom he will be putting.
- (f) Can be used for giving gifts to visiting NRI relatives. The amount should be credited to their NRO accounts.

7.9 The following transactions are prohibited under LRS:

Foreign Exchange

- (a) Remittance for any purpose specifically prohibited under Schedule-I and Schedule II.
- (b) Remittance from India for margins or margin calls to overseas exchanges/ overseas counterparty.
- (c) Remittances for purchase of FCCBs issued by Indian companies in the overseas secondary market.
- (d) Remittance for trading in foreign exchange abroad.
- (e) Remittances directly or indirectly to Nepal, Bhutan, Pakistan and Mauritius.
- (f) Loans can be given to close relatives, close relative as defined in Companies Act, 2013 by way of crossed cheque or electronic transfer within India subject to:
 - (i) The loan is free of interest.
 - (ii) Minimum maturity of the loan is one year.
 - (iii) Should be in the overall limit of USD 250000.
 - (iv) Should be used for personal requirements/ business purposes in India.
 - (v) Loan should be credited to NRO account.
 - (vi) The amount shall not be remitted outside India.
 - (vii) Repayment of the loan should be through inward remittance or debit to NRE/ NRO/ FCNR accounts of the Non-Resident Indian.

Capital Account Transactions

- 7.10 Person resident in India is allowed to conduct the following transaction with the Authorized Dealer under Capital account subject the limits specified therein.

Sale and purchase of foreign currency

- (i) A person travelling abroad can purchase foreign currency not exceeding USD 3000 or its equivalent if he is travelling to any country other than Iraq and Libya in which he is allowed to purchase foreign currency not exceeding USD 5000. In the case of travel to Islamic Republic of Iran Russian Federation and other republics of Commonwealth of independent states entire eligible amount can be carried in currency.
- (ii) For travellers proceeding for Haj/ Umrah pilgrimage, full amount of BTQ entitlement (Maximum USD 250,000) in cash or up to the cash limit as specified by the Haj Committee of India, may be released by the ADs and FFCs.
- (iii) Drawal of Foreign currency for any person for travel to Nepal and/ or Bhutan is prohibited. Rupee currency of denomination ` 100 and below without any limit and for denominations ` 500 and ` 2000 can be taken subject to maximum of ` 25000.
- (iv) The traveller should commence journey not later than 60 days from the sale of foreign currency.
- (v) Remittances for tour arrangements, purchase of Euro Rail pass can be given before commencement of journey.
- (vi) Unspent currency should be surrendered within 180 days from the date of return. The amount may be sold to AD or held in RFC account or use to discharge a debt or liability in Foreign Currency.
- (vii) Unspent cheques be surrendered within 180 days. However, currency up to USD 2000 and unlimited coins can be retained by the traveller on return.
- (viii) Unspent foreign currency can be utilized for subsequent journey.
- (ix) In case of cancellation of journey entire foreign exchange should be returned.
- (x) The unspent money can be credited to Resident Foreign Currency (Domestic) account.
- (xi) In all other cases, such as remuneration, income on assets held outside India, inheritance, settlement, gift, tips received in India in foreign currency, should be surrendered within 7 days to Authorized Dealer.

- (xii) The Holder of Foreign Currency must produce evidence for holding the foreign currency, i.e., purchase of foreign currency from the Authorised dealer to the Customs authorities / Police authorities or any Government Department, if asked.
- (xiii) Few people used to Purchase foreign currency from Unauthorised persons or from unauthorized dealers, and this action of purchase is Banned in India.

Import of Foreign Currency

- (a) A person coming to India may bring foreign currency without any limit subject to that if the currency notes, travellers' cheques exceed USD 10,000 a declaration in CDF is required, out of which foreign currency notes should not exceed USD 5000.
- (b) The person coming to India may also bring Indian currency not exceeding ` 25000 per person.
- (c) The person coming to India from Pakistan and Bangladesh, the India currency should not exceed "10000".
- (d) There is No such restriction of Indian Currency to persons return from Nepal and Bhutan and the denomination should not be above `100.

Export of Foreign Currency

A person going abroad can take outside India other than to Nepal and Bhutan an amount not exceeding Rs. 25000 per person. He may take not more than two commemorative coins and export of antique coins are allowed. Gift articles not exceeding value of Rs. 5 lakhs can be sent/ taken along with him. There are no restrictions on carrying jewellery, which are subject to customs guidelines.

Note

- (a) By declaring the Foreign Currency/Indian Currency in the Currency Declaration Form (CDR) anybody can take any amount out of India / Brought into India.
- (b) The above ceilings discussed above in Import of currency and Export of currency are without mentioning in CDR.
- (c) But Customs authorities/Police can ask for the source of holding the

foreign currency/ Indian currency from the holders of that currency at any time. It is not only at Airport/Ship, but at any place in case if they have got any doubt.

- (d) It is advisable to have proper records of holding the foreign currency in India by anyone including foreign nationals.

Acquiring Foreign Securities

7.11 A person resident in India may acquire foreign securities in the following manner:

- (a) By way of gift from a person resident outside India.
- (b) Issued by a company incorporated outside India under Cashless Employees Stock Option Scheme provided it does not involve any remittance from India.
- (c) By way of inheritance from a person whether resident in or outside India.
- (d) Purchased out of funds held in RFC accounts.
- (e) Bonus shares of the foreign securities held.
- (f) By investing under Liberalized Remittance facility.

Acquisition and Transfer of Immovable Property Outside India

7.12 The following are the cases on acquisition and transfer of immovable property outside India:

- (i) A person resident in India can hold, own, transfer or invest in any immovable property situated outside India if such property was acquired, held or owned by him when he was resident outside India or inherited from a person resident outside India.
- (ii) A person resident in India can receive as gift or inheritance from persons referred above.
- (iii) A person resident in India can acquire property through purchase from remittance under LRS/ RFC.

For these regulations, Relative means husband, wife, brother, sister or any lineal ascendant or descendant of that individual.

- (iv) Acquisition or transfer of immovable property outside India by a person resident in India would require RBI permission except when:
 - (a) property was held outside India by a foreign citizen resident in India.
 - (b) property acquired by a person or before 8.7.1947 and held with permission of RBI.
 - (c) property acquired by way of gift or inheritance from Persons referred in (b) above.
 - (d) property purchased out of funds held in RFC account.
 - (e) property acquired jointly with a relative who is a person resident outside India provided there is no outflow of funds from India.
 - (f) property acquired by way of inheritance or gift from a person resident in India who acquired such property abroad as per FEMA guidelines.

Borrowing from Non-Resident Indian in Foreign Currency

- a. Person resident in India is allowed to borrow Maximum amount USD 250,000 from a close relative as defined in Companies Act, 2013 subject to the minimum maturity of the loan is One year and the loan amount has been received as Inward remittance or debit to NRE / FCNR account, and no interest is payable on the loan amount.
- b. Section 2(77) of the Companies Act 2013 covers the following persons under "Relative" Definition:
 - A. Member of HUF
 - B. Husband
 - C. Wife
 - D. Father
 - E. Stepfather
 - F. Mother
 - G. Stepmother
 - H. Son

- I. Stepson
- J. Wife
- K. Daughter
- L. Daughter's Husband
- M. Brother
- N. Stepbrother
- O. Sister
- P. Stepsister
- Q. Stepdaughter (not included)

Borrowing from Non-Resident Indian in Rupees

- (a) Person resident in India is allowed to borrow from a non-resident as loan if the amount is received as inward remittance or debit to NRE/FCNR account of the non-resident.
- (b) The period of loan not to exceed three years and the rate of interest shall not be more than 2% over bank rate.
- (c) The amount repaid cannot be repatriated, however the same may be allowed to be credited to NRI NRO account.

Investments in Joint Ventures and Wholly Owned Subsidiaries Abroad

7.13 The following are the applicable points:

- (i) Indian parties are prohibited from making investment in a foreign entity engaged in real estate (meaning buying and selling of real estate or trading in Transferable Development Rights (TDRs) but does not include development of townships, construction of residential/commercial premises, roads or bridges) or banking business, without the prior approval of the Reserve Bank.
- (ii) An Indian party means a company incorporated in India or a body created under an Act of Parliament, or a partnership firm registered under the Indian Partnership Act, 1932 or a Limited Liability Partnership (LLP) incorporated under the Limited Liability Partnership Act, 2008,

making investment in a Joint Venture or Wholly Owned Subsidiary abroad.

- (iii) The Indian party/ entity may extend loan/ guarantee only to an overseas JV/ WOS in which it has equity participation.
- (iv) The Indian party should not be on the Reserve Bank's Exporters' caution list/ list of defaulters to the banking system.
- (v) All transactions relating to a JV/ WOS should be routed through one branch of an Authorized Dealer bank to be designated by the Indian party.
- (vi) Investments in Nepal are permitted only in Indian Rupees. Investments in Bhutan are permitted in Indian Rupees as well as in freely convertible currencies.
- (vii) Investments in JV/ WOS abroad by Indian parties through the medium of a Special Purpose Vehicle (SPV) are also permitted.
- (viii) Setting up of an SPV under the Automatic Route is permitted for the purpose of making an investment in JV/ WOS overseas.
- (ix) Investment in an overseas JV/ WOS may be funded out of one or more of the following sources:
 - (a) Drawl of foreign exchange from an AD bank in India.
 - (b) Capitalization of exports.
 - (c) Swap of shares.
 - (d) Proceeds of External Commercial Borrowings (ECBs)/ Foreign Currency Convertible Bonds (FCCBs).
 - (e) In exchange of ADRs/ GDRs issued in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993, and the guidelines issued there under from time to time by the Government of India.
 - (f) Balances held in EEFC account of the Indian party and
 - (g) proceeds of foreign currency funds raised through ADR/ GDR issues.

Opening of Foreign Currency accounts in India by Person Resident in India

- (a) Person resident in India is permitted to open the following types of accounts maintained in foreign currency.
- (b) Foreign currency account means an account held or maintained in currency other than the currency of India or Nepal or Bhutan.
- (c) Relative is a person as defined in section 2(77) of the Companies Act, 2013.
- (d) The accounts can be in the form of savings, current or term deposit where the account is an individual and in the form of current or term deposit in other cases.
- (e) In the case of EEFC, the account will be opened as per the scheme:
 - (1) Exchange Earners' Foreign Currency Accounts (EEFC).
 - (2) Resident Foreign Currency Account (Domestic).
 - (3) Resident Foreign Currency Account.
 - (4) Diamond Dollar Account.
 - (5) Accounts of SEZ.
 - (6) Other accounts.

The details of these accounts are given as under:

(a) Exchange Earners' Foreign Currency Accounts (EEFC)

1. EEFC account can be opened with 100 percent of the foreign exchange earnings received through inward remittance, payments received in foreign exchange by a 100 per cent Export Oriented Unit for goods supplied to such units or units in DTA, payments received in foreign exchange by a unit in Domestic Tariff Area for supply of goods to a unit in Special Economic Zone (SEZ), counter trade payments, advance remittance received for making exports, professional earnings including director's fees, consultancy fees, lecture fees, honorarium and similar other earnings received by a professional by rendering services in his individual capacity, payments received in foreign exchange by an Indian startup, and/ or re-credit of un-utilized foreign currency earlier withdrawn from the account.

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2. However, foreign currency loan raised, or investment received from outside India or those received for meeting specific obligations by the account holder cannot be credited to this account.
3. EEFC account can be used for making payments outside India towards for any capital or current account transactions permitted under Schedule II and III under FEMA, payment in foreign exchange towards cost of goods purchased from a 100 percent Export Oriented Unit, payment of customs duty, trade related loans/ advances, by an exporter account holder to his importer customer outside India, payment in foreign exchange to a person resident in India for supply of goods/ services including payments for air fare and hotel expenditure.
4. Withdrawal of rupees is permitted from this account, provided the amount withdrawn cannot be re-credited to the account.
5. The account will be in the form of a non-interest-bearing account.
6. The claims settled in rupees by ECGC/ insurance companies should not be credited to the account.
7. The total of the accruals in the account during a calendar month should be converted into rupees on or before the last day of the succeeding calendar month after adjusting for utilization of the balances for approved purposes or forward commitments.
8. Fund-based/ non-fund-based credit facilities should not be granted against the balances held in EEFC Accounts.
9. Exporters can repay packing credit advances, whether availed of in rupee or in foreign currency, from balances in their EEFC account to the extent exports have taken place.
10. Balances held in the account may be credited to NRE/ FCNR (B) Accounts, at the option/ request of the account holder's consequent upon change of their residential status from resident to non-resident.

(b) Resident Foreign Currency Account (Domestic)

1. A person resident in India who has gone abroad and acquired foreign exchange payment for services while on a visit to any place outside India:
 - (i) by way of gift or for service rendered to any person not resident in India while visit to India.

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- (ii) by way of honorarium or gift while on a visit to any place outside India.
 - (iii) in the form of unspent amount which he had taken while on visit to a foreign country.
 - (iv) received as from a relative.
 - (v) the amount represents disinvestment proceeds of ADR/ GDR.
 - (vi) settlement of Insurance policy claims in Foreign Currency.
2. The amount kept in the account can be utilized for the purpose of payments towards a current account and capital account transactions.
 3. If the person resident in India is going abroad and draws amount under LRS scheme the amount kept under this account shall be drawn over and above his entitlement.
 4. The account shall be maintained in the form of a Current Account and shall not bear any interest.
 5. There shall be no ceiling on the balances in the account.
 6. The total of the accruals in the account during a calendar month should be converted into rupees on or before the last day of the succeeding calendar month after adjusting for utilization of the balances for approved purposes.

(c) Resident Foreign Currency Account (RFC)

1. Non-resident Indians and PIO who are settling for good in India can open Resident Foreign Current Account with an authorized dealer.
2. A person resident in India is permitted to open an RFC account out of foreign exchange received or acquired by him:
 - (i) as pension or superannuation benefits from his overseas employer.
 - (ii) by converting assets which were acquired by him when he was a non-resident or inherited from or gifted by a person resident outside India and repatriated to India.
 - (iii) received as proceeds of LIC claims/ maturity/ surrendered value settled in forex from an Indian insurance company permitted to undertake life insurance business by the Insurance Regulatory and Development Authority.

3. The balances in the RFC account are free from all restrictions regarding utilization of foreign currency balances outside India.
4. Such accounts can be held jointly with resident relative as joint holder on 'former or survivor' basis. However, such resident Indian relative joint account holder cannot operate the account during the lifetime of the resident account holder.
5. The balances in the Non-Resident External (NRE) Account and Foreign Currency Bank [FCNR (B)] Account can be credited to the RFC account when the residential status of the non-resident Indian (NRI) changes to that of a Resident. The account can be opened as Savings Bank, Current or Term Deposit Account as offered by the Authorized Dealer.

(d) Diamond Dollar Account

1. Firms and companies dealing in purchase/ sale of rough or cut and polished diamonds/ precious metal jewellery plain, minakari and/ or studded with/ without diamond and/ or other stones with good track record of at least 2 years in import/ export of diamonds/ colored gemstones/ diamond and colored gemstones studded jewellery/ plain gold jewellery and having an average annual turnover of ` 3 crores or above during the preceding three licensing years are allowed to open Diamond Dollar Accounts up to five accounts with an authorized dealer.
2. The DDA shall be opened in the name of the exporter and maintained in US Dollars only.
3. The account shall only be in the form of a current account and no interest should be paid on the balance held in the account.
4. No intra-account transfer should be allowed between the DDAs maintained by the account holder.
5. Exporter firms and companies maintaining foreign currency accounts, excluding EEFC accounts, with banks in India or abroad, are not eligible to open Diamond Dollar Accounts.
6. A specific Application in prescribed form by Reserve Bank of India should be obtained while opening these accounts. Permitted credits to the account include the following:
 - (i) amount of pre-shipment and post-shipment finance availed in US Dollars.

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- (ii) Realizations of export proceeds from shipments of rough, cut, polished diamonds and diamond studded jewellery.
- (iii) realization in US Dollars from local sale of rough, cut and polished diamonds.

Permitted debits to the account include:

- (i) payment for import/ purchase of rough diamonds from overseas/ local sources.
- (ii) payment for purchase of cut and polished diamonds, coloured gemstones and plain gold jewellery from local sources.
- (iii) payment for import/ purchase of gold from overseas/ nominated agencies and repayment of US Dollars loans availed from the bank.
- (iv) transfer to rupee account of the exporter.

(e) Accounts for SEZ

1. Units located in SEZ are allowed to do foreign currency accounts with authorized dealer with foreign exchange funds received by the unit.
2. No foreign exchange purchased in India against rupees shall be credited to the account without prior permission from the Reserve Bank.
3. The funds held in the account shall be used for bona fide trade transactions of the unit in the SEZ with the person resident in India or otherwise.
4. The funds held in these accounts shall not be lent or made available in any manner to any person or entity resident in India not being a unit in Special Economic Zones.

(f) Other Accounts

1. Person's resident in India is allowed to open foreign currency accounts outside India.
2. Reserve Bank of India permits the following persons to open the accounts:
 - By a company for its office / branch.
 - For making overseas direct investment.

- Startup Companies.
 - Pending utilization of ADR/GDR/ECB funds.
 - Students who have gone abroad for studies.
 - Residents under LRS Scheme.
 - A shipping company incorporated in India.
 - Persons who have gone abroad for participation in exhibitions/fairs.
 - Person who has gone on temporary visit abroad.
3. However, as soon as the purpose for which the account has been opened has been completed, complied, the funds held in these accounts should be immediately repatriated to India.
 4. When a person resident in India leaves India for Nepal and Bhutan for taking up employment or for carrying on business or vocation or for any other purpose indicating his intention to stay in Nepal and Bhutan for an uncertain period, his existing account will continue as a resident account.
 5. Such an account should not be designated as a Non-resident (Ordinary) Rupee Account. In terms of Regulation 4(4) of the Notification No. FEMA.5/2000-RB dated May 3, 2000, ADs may open and maintain Rupee accounts for a person resident in Nepal and Bhutan.

Capital Account Transactions for Persons Resident outside India

Non-Resident

- (a) The term Non-resident or Non-resident Indian has not been defined in the FEMA.
- (b) Reserve Bank of India has defined the term Non-resident and Non-resident Indian in its various regulations issued from to time.
- (c) In certain regulations, the term Non-resident Indian includes Persons of Indian Origin also.
- (d) The following definitions, normally, give an understanding of these two terms - non-resident Indian and Person of Indian Origin.

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- (e) The concept of NRI for the purpose of Income Tax guidelines are different from regulations given by the Reserve Bank of India.
- (f) One must understand the NRI definition is different from the definition given as per the regulations of RBI.
- (g) Non-resident Indian means a person resident outside India who is a citizen of India or is a person of Indian origin.
- (h) This definition holds goods for various regulations issued by RBI namely, Foreign Exchange Management (Deposit) Regulations, 2000, Foreign Exchange Management (Investment in Firm or Proprietary concern in India) Regulations, 2000, Foreign Exchange Management (Transfer or Issue of Security by a person resident outside India) Regulation, 2000.
- (i) However, for the purpose of Foreign Exchange Management (Remittance of Assets) Regulation 2000, NRI means a person resident outside India who is a citizen of India.

Person of Indian Origin (PIO)' is a person resident outside India who is a citizen of any country other than Bangladesh or Pakistan, or such other country as may be specified by the Central Government, satisfying the following conditions:

- (a) Who was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955 (57 of 1955); or
- (b) Who belonged to a territory that became part of India after the 15th day of August 1947; or
- (c) Who is a child or a grandchild or a great grandchild of a citizen of India or of a person referred to in clause (a) or (b); or
- (d) Who is a spouse of foreign origin of a citizen of India or spouse of foreign origin of a person referred to in clause (a) or (b) or (c).

Explanation: PIO will include an 'Overseas Citizen of India' cardholder within the meaning of Section 7(A) of the Citizenship Act, 1955

7.14 As FEM (Deposit) Regulations, 2000 have been repealed and replaced by FEM (Deposit) Regulations, 2016 with effect from April 1, 2016 (FEMA 5(R)), the term NRI, wherever it appeared, has been replaced by NRI and/or PIO. Prior to this, PIOs were covered within the definition of NRI.

Facilities available for NRIs and PIOs

7.15 Both NRIs and PIOs can open various deposit accounts with authorised dealers as per guidelines given by Reserve Bank of India from time to time.

A comparative chart of all the deposit schemes is given hereunder:

	FCNR	NRE	NRO
ELIGIBILITY	NRIs.	NRIs.	NRIs
	Residents of Bangladesh/Pakistan nationality/ownership require approval of RBI	Residents of Bangladesh/Pakistan nationality/ownership require approval of RBI.	Residents of Bangladesh/Pakistan nationality/ownership require approval of RBI. In the case of Bangladesh, AD can open provided he has valid visa, and valid residential permit issued by Foreign Registration Office.
			Foreign Nationals are also allowed to open accounts.
TYPES OF ACCOUNTS	Only Term Deposit Accounts - cumulative or non-cumulative.	Savings Bank and Current Accounts, TDR accounts cumulative or non-cumulative	All types of accounts allowed included. Current Deposit Accounts.
	Accepted in permitted currency which is fully convertible. For	cumulative, RD accounts allowed. Remittance can be received in	Remittance can be received in any currency and some local credits allowed. Maintained in Indian

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	example: USD, GBP, EUR, AUD. (Some banks accept additional currencies also)	any currency, but the account maintained in Indian Rupees.	Rupees.
PERIOD OF DEPOSIT AND RATE OF INTEREST JOINT ACCOUNTS	PERIOD Minimum 1 year. Maximum 5 years. RATE OF INTEREST 1 to < 3 yr – LIBOR + 200 bps. 3 to 5 yrs – LIBOR + 300 bps. LIBOR is given by FEDAI monthly.	PERIOD TDRs Minimum one year. Maximum 10 years. RATE OF INTEREST As decided by individual Banks. ROI should not be more than domestic deposits.	PERIOD TDRs Minimum 7 days. Maximum 10 years as applicable to domestic deposits. RATE OF INTEREST As decided by individual banks. Rates as applicable to domestic deposits.
	Individuals, two or more NRIs	Individuals, two or more NRIs	Individuals, two or more NRIs.
	Individuals. Joint Account with Resident close relatives on F or S basis.	Individuals. Joint Account with Resident close relatives on F or S basis.	Joint account can be opened with NRIs and / or Indian Residents. Operational instructions, E or S,

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			F or S, or Any or
	NO Income Tax on interest	NO Income Tax on interest	S. Tax at 30.9% to be deducted on interest. In case DTAT countries appropriate tax will be deducted.
NOMINATION	NRI / RESIDENT ALLOWED. In the event of the demise of the account holder, the balances in the account can be transferred to the non-resident nominee. If a resident nominee requests for Remittance of funds outside the country to meet the liabilities of the NRI, RBI permission is required. Allowed in any currency	NRI / RESIDENT ALLOWED. In the event of the demise of the account holder, the balances in the account can be transferred to the non-resident nominee. If a resident nominee requests for remittance of funds outside the country to meet the liabilities of the NRI, RBI permission is required. Allowed in any currency.	NRI / RESIDENT ALLOWED. In the event of the demise of the account holder, the balances in the account can be transferred to the non-resident nominee. If a resident nominee requests for remittance of funds outside the country to meet the liabilities of the NRI, RBI permission is required.
REPATRIATION OF FUNDS			Allowed with restrictions. i) Current Income

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			and Interest.
			ii) Up to USD 1 Mn. per financial year for any Bonafide purposes / sale proceeds of assets.
POWER OF ATTORNEY	Allowed for repatriation of funds to depositor.	Allowed for repatriation of funds to depositor.	Allowed for repatriation of funds to depositor. Local Payments. Remittances outside India from current income in India.
INTERNATIONAL CREDIT CARDS	International Credit cards can be given to all NRIs.	International Credit card / Debit Card / Cheque Books for SB accounts.	International Credit card / Debit Card / Cheque Books for SB accounts.
PERMISSIBLE CREDITS	Inward remittance for creation of the deposit	Inward remittance. Interest accrued on the account. Interest on investment.	Inward remittances. Legitimate dues in India. Rupee gift / loan given. by a resident under LRS Scheme.
		Transfer from other NRE/ FCNR accounts.	
		Current income like rent,	

Foreign Exchange

		dividend, pension, interest etc.	
PERMISSIBLE DEBITS	Repatriation funds on maturity of the deposit. Transfer funds to NRE / NRO account. Meeting Local payments in Indian rupees	Local payments. Remittances outside India. Transfer to NRE/FCNR accounts.	Local payments. Transfer of current income abroad (over and above USD one million) Up to USD 1 Mn. per financial year for any Bonafide purposes / sale proceeds of assets.
			Funds can be transferred to NRE account within USD 1 million.
LOANS IN INDIA IN RUPEES AGAINST TDRS	Account Holder / Third Party Allowed	Account Holder / Third Party Allowed	Account Holder / Third Party Allowed
LOANS IN FOREIGN CURRENCY AGAINST TDRS	Account Holder / Third Party Allowed	Account Holder / Third Party Allowed	NOT PERMITTED
PURPOSE OF LOAN	Personal purposes or for carrying on business activities Direct investment in	Personal purposes or for carrying on business activities Direct investment in India on non-	Personal requirement / Business purpose. Loan cannot be sanctioned for relending, carrying on agricultural/

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	India on non-repatriation basis by way of contribution to the capital of Indian firms / companies	repatriation basis by way of contribution to the capital of Indian firms / companies	plantation activities or investment in real estate.
	Acquisition of flat / house in India for his own residential use.	Acquisition of flat / house in India for his own residential use.	

Guidelines for Loans against NRI Deposits

- A. Authorised Dealers/ banks in India can grant loans against the security of the funds held in NRE accounts to the account holder/ third party in India, without any limits, subject to the usual margin requirements.
- B. The loan cannot be repatriated outside India and shall be used for the following purposes:
 - a) personal purposes or for carrying on business activities except for the purpose of relending or carrying on agricultural/ plantation activities or for investment in real estate business.
 - b) making direct investment in India on non-repatriation basis by way of contribution to the capital of Indian firms/ companies subject to the provisions of the relevant Regulations made under the Act.
 - c) acquiring flat/ house in India for his own residential use subject to the provisions of the relevant Regulations made under the Act.
- C. In case of loans sanctioned to a third party, there should be no direct or indirect foreign exchange consideration for the non-resident depositor agreeing to pledge his deposits to enable the resident individual/ firm/ company to obtain such facilities.
- D. In case of the loan sanctioned to the account holder, it can be repaid either by adjusting the deposits or through inward remittances from outside India through banking channels or out of balances held in the

NRO account of the account holder.

- E. Authorized Dealers may allow their branches/ correspondents outside India to grant loans to or in favour of non-resident depositor or to third parties at the request of depositor for bona fide purpose against the security of funds held in the NRE accounts in India and agree for remittance of the funds from India, if necessary, for liquidation of the outstanding.
- F. The facility for premature withdrawal of deposits will not be available where loans against such deposits are availed of.
- G. The term "loan" shall include all types of funds based/ non fund-based facilities.
- H. Loans against security of immovable property or shares can be allowed to NRIs in India rupees.
- I. However, the purpose of loans should be to meet personal expenses.
- J. The amount cannot be credited to NRE / FCNR accounts, and no repatriation is allowed.
- K. The repayment of these loans should be through inward remittance or to the debit of NRE / FCNR account.

Investment in Shares and Securities

- a. A Non- Resident Indian (NRI) may acquire securities or units on a Stock Exchange in India on repatriation basis under the Portfolio Investment Scheme, subject to the terms and conditions specified in Schedule 3. A Non- Resident Indian (NRI) may acquire securities or units on a non-repatriation basis, subject to the terms and conditions specified in Schedule 4.
- b. For this purpose, the NRI is required to open a special account called NRE (PIS) account with an authorised dealer who is offering such accounts.

Acquisition and Transfer of Property in India

- a. These guidelines are applicable to both Non-resident Indians and Persons of India Origin.
- b. NRI can acquire property in India by:
 - (i) purchase of immovable property (other than agricultural

land/plantation property /farmhouse) and

- (ii) Transfer of immovable property. (Transfer includes sales, purchase, mortgage, exchange, pledge, gift, loan or any other form of transfer of right, title, possession or lien). In case the residential property so purchased is sold, the purchase price can also be permitted to be repatriated, and the balance amount has to be credited to NRO account, and such repatriation is allowed only in the case of two properties.
- (iii) In case property is purchased through rupee funds an amount up to USD 1 Mn is allowed to be repatriated in a financial year after obtaining permission from Reserve Bank of India.
- (iv) In case property in India has been acquired while the status of the NRI remains as NRI, an amount up to USD 1 Mn is allowed to be repatriated in a financial year after obtaining permission from Reserve Bank of India.
- (v) In case property has been acquired while the status of the NRI was person resident in India, RBI permission is required to repatriate the funds.
- (vi) The NRI is allowed to transfer the property held in India to a person resident in India, or another NRI, PIO.
- (vii) But transfer of property to foreign national is not allowed.

Other Remittance Facilities for NRIs/ PIOs

- a. Current income like rent, dividend, etc., can be remitted outside India and the same can also be credited to NRE account.
- b. They are also permitted to remit up to USD 1 Mn. per year funds held in NRO ac/sale proceeds of immovable property purchased by him out of rupee funds or acquired through inheritance without any lock in period.
- c. However, this facility is not available for citizens of Pakistan, Bangladesh, Sri Lanka, China, Afghanistan, Iran, Nepal and Bhutan.

Foreign Nationals

- a. Foreign nationals of non-Indian origin on a visit to India can open NRO – CD/ SB accounts for a maximum period of six months.

Foreign Exchange

- b. Funds should be received through Banking channels.
- c. This facility is not for citizens of Nepal and Bhutan.
- d. On return of the foreign national, the funds can be repatriated subject to account has been maintained for a period not exceeding six months and the account has not been credited with any local funds, other than interest accrued thereon. RBI approval required for accounts above six months.
- e. Foreign nationals of non-Indian origin resident outside India cannot acquire any property in India unless such property is acquired by way of inheritance from a person who was resident in India. They can acquire on lease for five years without permission from RBI.
- f. Citizens of Pakistan, Bangladesh, Sri Lanka, Afghanistan, China, Iran, Nepal, Bhutan, Macau or Hong Kong cannot, without prior permission of the Reserve Bank, acquire or transfer immovable property in India, other than lease, not exceeding five years.
- g. Foreign nationals' resident in India can open and maintain resident rupee accounts.
- h. On return, their accounts should be re-designated as NRO to enable pending funds to be credited to the account.
- i. On retirement from India, they are permitted to remit USD 1 Mn from his NRO account every year. They have been, however, permitted to maintain a foreign currency account outside India and remit his salary to that account.

Requirements under Income Tax Act

Section 195 (6) of Income Tax Act, 1961, requires the person paying to NRI to furnish the information as per Rule 37 BB. Information should be submitted to Income Tax if paying to a non-resident, not being a company or to a foreign company in FORM 15 CA AND 15 CB.

Import of Goods and Services

- a. In addition to Exchange Management controlled by Reserve bank of India in respect of import of goods and services, one should be familiar with trade management guidelines governing the imports.

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- b. It is also necessary that one should be familiar with the internal guidelines of the Bank as major areas like, assessment of limits, obtention of securities, documentation, interest rates and service charges, opening of Letters of Credit, issuance of guarantee, standby letters of credit are governed by internal guidelines of each bank.
- c. One should also be familiar with ICC guidelines governing Letters of Credit – Uniform Customs and Practices - UCP600, Standby Letters of Credit – ISBP 98, Uniform Rules for Collection – URC 522, Uniform Rules for Demand Guarantees – URDG 758, INCOTERMS 2010, etc.

Guidelines under Trade Control

- a. Both imports and exports are controlled by Ministry of Commerce and Industry through Director General of Foreign Trade (DGFT).
- b. Government of India releases Foreign Trade Policy (FTP) which is applicable for a period of five years and the present policy is for the period 2023-28, which comes into effect from 01.04.2023.
- c. As per the FTP policy guidelines, any person conducting the business under imports and exports should first have IEC number obtained from DGFT.
- d. All items are classified as those which may be freely imported, restricted, canalized or prohibited.
- e. Authorized Dealers may freely open Letters of Credit and allow remittances for import of goods unless they are included in the restrictive list requiring license under the Foreign Trade Policy in force.
- f. In such cases, letters of credit should be opened only against valid import licenses marked "For Exchange Control Purposes".

Reserve Bank of India Guidelines on Import of Goods and Services

- a. The authorised dealers who are conducting transactions for importers must ensure that the importer has obtained valid IEC (Import-Export Code) number from DGFT.
- b. The goods being imported if categorized under restricted category needs license issued by DGFT and a copy marked as "for Exchange Control purposes" has been obtained and kept on record.

- c. The banks should also ensure that the Importer holds a confirmed order executed between the importer and supplier of goods.
- d. The branches should meticulously follow KYC guidelines issued by RBI from time to time regarding opening, monitoring and scrutinizing the transactions of importers.
- e. Branches should obtain a declaration in FORM-1, when the importer/exporter regularly deal with the bank and to be obtained once. In case the dealings of importer are occasional or casual in nature FORM II should be obtained.
- f. Whenever payments are required to be made by Authorised Dealer, the importer is required to submit his request in FORM – A – 1 which has been since dispensed with by Reserve Bank of India. However, a suitable declaration should be obtained with proper supporting documents.
- g. Banks are required to make payments for importers in respect of import transactions in the following circumstances:
 - (i) Payments towards receipt of bills under Letter of credit opened by them on behalf of the importer favouring foreign supplier/ bank.
 - (ii) Advances remittances for imports as required by the supplier.
 - (iii) Payment towards realization of bills received under collection from the Seller /his bank.
 - (iv) Outward remittances for direct imports.

Settlement of Import Payments

- a. All import payments, normally, should be settled within a period of six months from the date of shipment.
- b. In case of delayed settlement, Authorized Dealer can allow payment of interest up to 3 years.
- c. Extension in period of payment should be given 6 months at a time.
- d. In case extension is given beyond one year, the total outstanding of the importer does not exceed USD one Million or 10% of the average import remittances during the preceding two financial years, whichever is lower.

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- e. There is no time limit for payment of import of books.
- f. Interest payment may be made in case payments are made later.
- g. The Authorized Dealer should be satisfied of such delayed payment.
- h. Importer may withhold 15% from import payments as per the terms of purchase agreement between the importer and the seller. This may be paid without interest later.

Trade Credits

- a. In case deferred payment arrangements, such as, Suppliers' and Buyers' credit are made by the importer such payments are covered under Trade Credits.
- b. In case of trade credits (which are covered under ECB guidelines) the maximum amount allowed is USD 20 MN, up to one year for non-capital goods and up to 5 years for Capital Goods per import transaction in all sectors from date of shipment.
- c. In case trade credit has been sanctioned no rollover/extension is permitted.
- d. The all-in cost for payment of Interest should not exceed 6 months LIBOR + 350 bps. AD is permitted to issue guarantee for payment of trade credits up to a period of 3 years.

Third Party Payments for Imports

- a. Sometimes the importers may require making payments to third party who is other than the seller of the goods.
- b. In such cases third payment payments are allowed subject to a firm irrevocable purchase order/ tripartite agreement is in place between the importer, seller and the third party (normally, the supplier of goods) and authorized dealer is satisfied with the Bonafide of the transactions and should consider the Financial Action Task Force (FATF) statement before handling the transactions.
- c. The Invoice should contain a narration that the related payment must be made to the (named) third party.
- d. Bill of Entry should mention the name of the shipper as also the narration that the related payment must be made to the (named) third party.

Advances Remittances

- a. The seller may request the importer to arrange for advance remittance after execution of purchase order and before shipment of the goods.
- b. Authorized dealers may entertain such requests from importer customers subject to:
 - (i) the importer holds a valid import license if license is required for such import.
 - (ii) a confirmed order is in place between the supplier and the importer.
 - (iii) advance remittance is made directly to supplier.
- c. The AD banks may not insist guarantee from the supplier's bank up to an amount of advance remittance of USD 2,00,000.
- d. In case the amount exceeds USD 200,000 guarantee from international bank provided by the supplier is required.
- e. Individual Banks may waive the condition and make payment up to USD 1 Mn as per their Board approved policy.
- f. A declaration should be obtained as per Bank's Performa.

Advance Remittances for Import of Rough Diamonds

- a. The authorized dealer before making advance remittance for an importer who is dealing in import of rough diamonds must ensure that:
 - A. the overseas mining company has the recommendation of GJEPC (The Gem and Jewellery Export Promotion Council).
 - B. The importer should be a recognized processor of rough diamonds and should have a good track record.
 - C. AD Category - I bank should, undertake the transaction based on their commercial judgment and after being satisfied about the Bonafide of the transaction.
 - D. Advance payments should be made strictly as per the terms of the sale contract and should be made directly to the account of the company concerned.

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- b. Further, due caution should be exercised to ensure that remittance is not permitted for import of conflict diamonds (Kimberly Certification) and KYC and due diligence exercise should be done.
- c. Banks should follow-up submission of the Bill of Entry/ documents evidencing import of rough diamonds into the country by the importer.

Time Period for Shipment/ Payment Under Advance Remittances

- a. Goods should be imported within 6 months from the date of advance remittance for noncapital goods and 3 years for capital goods.
- b. The authorized dealer can allow an extension of one month for import of goods.
- c. In case of non- import, the advance payment if any made should be repatriated immediately.
- d. The balance amount of remittances for imports should be completed within six months from the date of shipment.

Procedure for Receipt of Import Bills/ Documents (otherwise than under Letter of Credit)

- a. Sometimes, as per the purchase order between the supplier and the importer, the bills will be sent by the seller to the importer's bank or importer directly, and if the bills are directly sent by the importer, he will request the authorised dealer to make payment there under.
- b. The following guidelines are applicable:
 - 1. Bills should be received directly from the supplier's bank. However, in some cases, Bills can be directly received from the supplier by the importer's bank (i) if where value of good imported does not exceed USD 300,000, (ii) bills received from wholly owned subsidiaries of foreign companies from their principals. (iii) if the importer is a Status holder exporter or 100%EOU/Units in Special Economic Zones, PSU and Limited Companies (iv) Bills received by all limited companies (iv) Bills can be directly received from the supplier if Bank is satisfied.

2. The bills received under collection by the Banks directly either from supplier's bank or the supplier are governed under Uniform Rules for Collection (URC 522) and hence should be guided by those rules. They should also ensure that the bills drawn under Letter of Credit are not sent under collection without being covered under URC 522.

Evidence of Import

- a. It is necessary that the authorized dealer ensures that importer submits evidence of import to the Bank in a reasonable time.
- b. The evidence of import depends upon the type of import and such Bills of Entry (BEF) should be obtained and kept on record at least for a period of one year after audit of the branch is completed.
- c. In no case, the original BEF should be returned to the importer by the authorized dealer.
- d. The authorized dealer is required to acknowledge receipt of BEF.
- e. As per the present guidelines BEF need not be submitted in case the import is up to an amount of USD 100,000 (Per importer Per Financial Year).
- f. In all other cases, the BEF should be submitted to the authorized dealer within a period of three months from the date of remittance for import.
- g. The authorised dealer may give an extension of three months for submission of such BEF and in case the same is not submitted even after the lapse of six months, the authorized dealer should report the same to RBI in the half-yearly return in June and December every year of all those pending BEFs over USD 100,000.
- h. In case, the payment is made for Bills received on DA terms, the evidence of import should be submitted before making the payment for the imports.
- i. It is advisable that the authorized dealer should verify the website, ICEGATE for genuineness of the BEF submitted by the importers.

Merchant Trade

- a. To qualify a transaction under merchant trade both conditions to be satisfied are:
 - A. goods acquired should not enter the Domestic Tariff Area and
 - B. the state of the goods should not undergo any transformation.
- b. In addition to that other conditions to be complied with under merchant trade are:
 - (i) goods to be imported/exported are permitted under FTP.
 - (ii) both legs of trade are routed through same Bank.
 - (iii) the entire transaction is completed within a period of 9 months.
 - (iv) the transactions do not involve foreign exchange outlay for a period exceeding four months.
 - (v) the commencement of Merchant Trade is the date of shipment / export leg receipt or import leg payment whichever is first.
 - (vi) payment is received in time for the export leg first.
 - (vii) Supplier's credit / buyer's credit is available to the extent advance remittance not received.
 - (viii) advance remittance for import leg permitted.
 - (ix) Letter of credit for the supplier permitted against confirmed export order.
 - (x) payment for import may be allowed from EEFC balances.
 - (xi) one to one matching of merchant trade should be ensured.
 - (xii) the merchanting traders should be genuine trader of goods.
 - (xiii) confirmed orders must be received from their buyers.
- c. The authorized dealer should ensure that (a) defaulting merchanting traders whose outstanding reach 5 % of their annual export earnings would be caution listed, (b) merchanting traders have to be genuine traders of goods and not mere financial intermediaries, (c) In case of Nepal and Bhutan are landlocked countries, Customs transit declarations have to be obtained.

Issue of Guarantee for Import of Services

- a. Authorized dealers are permitted to issue guarantees for import of services at the request of import customers in favor of non-resident service provider for amounts not exceeding USD 5,00,000.
- b. The guarantee is to secure a direct contractual liability arising out of contract between resident and non- resident.
- c. For issue of guarantee exceeding USD1,00,000 in respect of PS Company or Dept of GOI, MOF approval is required.
- d. If the guarantee is invoked, matter should be reported RBI.

Key points relating to various guidelines issued by RBI on Imports are narrated below:

- (i) Import Trade is regulated by the DGFT under the Ministry of Commerce & Industry. While the physical merchandize, concept is governed by the Foreign Trade Policy and implemented by the Customs Authorities, the foreign exchange part is governed under the FEMA regulations and implemented by the RBI through the Authorized Dealers.
- (ii) AD Banks should ensure that the imports into India are in conformity with the FTP in force (2009-14), FEMA rules 2000, adherence to the provisions of Income Tax Act, wherever applicable and directions by RBI from time to time.
- (iii) AD Banks should ensure normal banking procedures; KYC guidelines & adhere to the provisions of the UCP while opening LCs for imports into India. Where specific regulations do not exist, AD Banks may be governed by normal trade practices in all their dealings.
- (iv) Application for all Import payments exceeding USD 5,000/- towards Imports into India, should be supported by Form A1 and supported by documents(Import documents) to the satisfaction of the AD. AD Banks need not obtain any document including A-1 except a simple letter from the applicant containing the basic information, viz., the name and address of the applicant, name and address of the beneficiary, amount to be remitted, purpose of the remittance as long as the exchange being purchased is for a current account transaction.
- (v) Remittances against Imports should be completed not later than six months from the date of shipment. However, AD Banks may permit

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settlement of import dues delayed due to disputes, financial difficulties, etc., beyond the 180 days subject to the condition that the AD is satisfied with the reasons put forth by the Importer.

- (vi) Advance remittances towards Imports are allowed without any ceiling. However, if the amount exceeds USD 2,00,000 or its equivalent, such remittances should be supported by a bank guarantee. In cases where the Importer is unable to obtain the bank guarantee and the bank is satisfied about the track record and Bonafide of the transaction, bank may permit such advance remittances without insisting for a bank guarantee subject to maximum amount of USD 5 Mn. Banks to put in place a policy approved by the Board of the bank in this regard.
- (vii) The Importer is under obligation to submit the documentary evidence for having completed the Imports (Exchange Control Copy of the Bill of entry) within 6 months from the date of remittance in case of Advance Remittance. In respect of imports under D/A basis, the BOE should be submitted at the time of effecting the outward remittance and in case of D/P basis, the BOE must be submitted within 3 months from the date of remittance. In case of default in submission of the evidence of Import, for amounts exceeding USD 1 Lac, AD should report such transactions to RBI in BEF Statement on half yearly basis.
- (viii) For Imports with value of less than USD 1 Lac, Banks can insist for any other alternate document as documentary evidence for import in lieu of the Bill of Entry (subject to the Board approved policy of the Bank) that the goods have been imported along with reason for non-submission. the BOE.
- (ix) In respect of import of non-physical Imports, a certificate from a Chartered Accountant that the software/data/ drawing/design has been received by the Importer to be submitted to the AD.
- (x) Import of gold on consignment basis by nominated agencies/banks is permissible only to meet the genuine needs of Exporters of gold jewellery. Exports. LCs opened by nominated Banks/Agencies for import of gold will be only on 100 % cash margin and should be on documents against payment basis (DP basis).
- (xi) Imports can be handled in either of the following methods:
 - (a) Imports under Advance remittances-All advance remittances

exceeding USD 2 Lac to be supported by a bank guarantee. If the Importer is unable to provide the guarantee, bank based on the relationship can waive guarantee for amounts up to USD 5 Mn. and BOE be submitted within 6 months from date of remittance.

- (b) Letters of Credit-Letters of credit are a set of instructions given by the Importer and conveyed by the Importer's Banker to the Overseas Bank for onward transmission to the supplier with a commitment that payment under the LC will be made if the documents submitted are credit compliant. Opinion on the Overseas Supplier either through DNB or through a Banker is to be obtained. Before establishing the LC, credit processing and non-fund-based limits are to be put in place. As per RBI guidelines, all import LCs are to be established for a tenor not exceeding 180 days from date of shipment (in case of procurement of raw materials) and 3 years in case of procurement of capital goods. All transactions under LCs are governed under extant provisions of UCP 600 established by ICC.
- (c) Imports under Collection basis received by the Bank- Authorized dealers are to exercise due care while handling Import bills under Collection basis received on behalf of their Importers with reference to their line of business, financial standing, frequency of imports and track record to establish genuineness of imports. Satisfactory opinion report on the overseas supplier may be called for from the bankers, accredited rating agencies, etc., in support of the genuineness of the Import. Original documents received along with the Overseas Bank's covering letter to be thoroughly scrutinized to ensure adherence to the instructions contained therein. All transactions under collection are governed under the Uniform Rules for Collection – URC 522.
- (d) Import Bills received directly by the Importer- AD Banks may make remittances where import bills have been received by the Importers directly from the Overseas Supplier in respect of the following cases:
 - Value of the import bill does not exceed USD 300,000 or equivalent where the Importer is a sole proprietor, partnership or an LLP.

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- Import bills received by the WOS of Foreign Companies irrespective of the amount of the bill.
- Import bills received by status holder exporters, 100 % EOUs, Units in SEZs irrespective of the amount of the bill.
- Import bills received by PSUs irrespective of the amount of the bill.
- Import bills received by all limited companies (Public Limited, Deemed Public Limited and Private Limited Companies) irrespective of the amount of the bill.

Export of Goods and Services

The Foreign Exchange Management (Export of Goods and Services) Regulation, 2000, contains instructions regarding exports of goods and services and the same should be read with modifications made there under. Reserve Bank of India Master Direction no. RBI/FED/2015-16/11 FED Master Direction No. 16/2015-16 January 1, 2016 (updated up to 12.5.2016) consolidates all the directions issued there under. The concurrent auditor is requested to read the updated circulars issued by RBI after this circular

Declaration of Export of Goods and Services

- a. All exporters are required to declare the value of exports made under export declaration forms.
- b. There are three declaration forms, namely, Statutory Declaration Forms (SDF) issued by EDI (Export Data Interchange) ports which have been fully computerized. Export Declaration Forms (EDF) shall be issued by non – EDI ports.
- c. SOFTEX forms are used for software exports.
- d. PP (Post Parcel) form is used for export by post and VP/COD forms are used when goods are exported on Value Payable basis or Cash on Delivery basis.
- e. In case, the goods are exported in any of the situations, viz.:
 - (i) trade samples of goods and publicity material supplied free of payment.

- (ii) personal effects of travellers, whether accompanied or unaccompanied.
 - (iii) goods or software whose value is not more than Rs. 25,000.
 - (iv) by way of gift of goods not more than one lakh rupees in value.
 - (v) Aircrafts or aircraft engines and spare parts for overhauling and/or repairs abroad subject to their re-import into India after overhauling /repairs, within a period of six months from the date of their export.
 - (vi) goods imported free of cost on re-export basis.
 - (vii) goods not exceeding U.S.\$ 1000 or its equivalent in value per transaction exported to Myanmar under the Barter Trade Agreement between the Central Government and the Government of Myanmar.
 - (viii) The following goods which are permitted by the Development Commissioner of the Export Processing Zones or Free Trade Zones to be re-exported, namely, (a) imported Goods found defective, for the purpose of their replacement by the foreign suppliers/ collaborators, (b) goods imported from foreign suppliers/ collaborators on loan basis , (c) goods imported from foreign suppliers/collaborators free of cost, found surplus after production operations, (d) replacement goods exported free of charge in accordance with the provisions of Exim Policy in force.
- f. Authorized Dealer may waive submission of Declaration forms if (a) the export of goods is free of cost, (b) for export promotion up to 2% of average annual exports during preceding three financial years, subject to a maximum amount of ` 5 lakhs for non-status holders and 10% for status holders whichever is higher. However, export of goods not involving any foreign exchange requires Reserve Bank of India approval.
- g. Authorized Dealer may also approve submission of EDF for goods taken out for exhibition and participation in trade fairs subjects to (i) unsold exhibits may be sold outside the exhibitions, (b) unsold exhibits can also be gifted up to a value of USD 5000 per exporter, per exhibition/trade fair. The approval by authorized dealer is subject to (a) bill of entry produced within one month of re-import of unsold items, (b)

the sale proceeds are repatriated immediately and (c) the method of disposal of items should be reported to him. All such transactions are subject to 100% by auditors.

Submission of Documents by Exporters

- a. The exporter should submit all shipping documents (such as Bill of Lading, Insurance, invoice, etc.) along with declaration forms and other documents requested by the buyer to authorized dealer within 21 days from date of shipment.
- b. The documents may be submitted for negotiation if Letter of Credit has been established in favour of the exporter, and/ or for discounting of DA bills and purchase in case of DP bills.
- c. The authorized dealer should dispatch the documents to their overseas branches/ correspondents or as per LC instructions.
- d. The exporters are permitted to send the documents and can be directly sent to consignees provided:
 - Advance payment or an irrevocable letter of credit established for the full value and the sale contract provides dispatch of goods directly to them.
 - The exporter is regular customer of the AD Bank. (iii) where the value of export does not exceed USD 1 Mn.
- e. Status Holder exporter can directly dispatch the documents to the consignee provided the export proceeds are repatriated through AD named in EDF/SDF forms and the duplicate copy of EDF/SDF submitted within 21 days of shipment to AD.

Receipt of Payment for Exports

- a. There is no restriction on invoicing of export contracts in INR or in freely convertible currency, but export proceeds shall be realized in convertible currency only.
- b. The exporter must realize full value of the goods/ software/ services should be realized within a stipulated period from the date of export.
- c. The stipulated period for receipt of export proceeds in all cases is maximum nine months and in case goods are exported to warehouses outside India, the period of realization is 15 months.

Foreign Exchange

- d. Banks can allow extension of time beyond nine months for a period of six months provided:
 - 1. the export transactions are not under investigation.
 - 2. the exporter is unable to realize due to reasons beyond his control.
 - 3. exporter submits a declaration that the same will be realized during extended period.
 - 4. total outstanding of exporter does not exceed USD 1 Mn. or 10% of average realizations during preceding three years whichever is higher.
 - 5. all export bills outstanding beyond six months are subject to reporting under XOS statement.
 - 6. extension may be permitted without any time limit if a suit has been filed by the exporter on consignee.
 - 7. Any further extension of time beyond the time allowed by Authorized Dealer, is subject to approval by Reserve Bank of India.
- e. Payment should be received through authorized dealer by way of:
 - 1. Bank draft/personal cheque.
 - 2. to the debit of FCNR/ NRE accounts of consignee held in India.
 - 3. International credit cards.
 - 4. Through OPGSPs – Online Payment Gateway Service Providers with maximum amount of USD 10,000.
 - 5. FC/TC from buyer during his visit to India.
 - 6. In rupees/ ACU mechanism for Nepal and Bhutan.
 - 7. In precious metals, units set up in SEZs and EOUs equivalent to Jewellery exported.
- f. Other conditions governing receipt of payment for exports are, in case the payments are from ACU countries they must settle in ACU Dollar or ACU Euro.
- g. In the case of Myanmar, the payment can be received in other currencies also.

- h. Third Party payments for exports are permitted.
- i. Payment should be received in the currency appropriate to the place of destination irrespective of residence of buyer.

Advance Receipts

- a. Sometimes exporters may receive advance for the goods to be exported in future.
- b. In such cases, the export should be shipped within one year from receipt of advance payment.
- c. In case the export agreement states that the export can take place beyond one year from the receipt of advance receipt, approval of Authorized Dealer is required.
- d. In case agreements states so, exporter can pay interest on advance receipt at rate of interest not exceeding LIBOR + 100 bps.
- e. All the documents should be routed through the same authorized dealer through whom the advance has been received.
- f. In case shipment does not take place within one year from the receipt of advance, RBI approval is required to refund the remittance.

Reserve Bank of India permits to receive advance payments for longer periods up to 10 years allowed subject to:

- (i) Minimum of 3 years satisfactory track record of exporter.
- (ii) Firm orders for export are in place.
- (iii) Product pricing should be in consonance with prevailing prices.
- (iv) The company has capacity to execute such long-term orders.
- (v) No Enforcement Directorate notices were issued to the company.
- (vi) Rate of interest payable on such advance remittances does not exceed LIBOR + 200 bps.
- (vii) The documents should be routed through AD only.
- (viii) Such advance above USD100 Mn should be reported to RBI.
- (ix) In case the exporter request for issuance of BG/SBLC in favour of the consignee who has given advance payment, should not be issued for more than for 2 years and then *rolled over if requested by the exporter*.

Write Off

- a. The Authorized Dealers as well as exporters are permitted to write off unrealized export bills subject to limits specified by the Reserve Bank of India.
- b. Such write off is permitted only in the cases where:
 - 1. the write off is outstanding more than one year.
 - 2. the overseas buyer has been declared as insolvent.
 - 3. the whereabouts of the overseas buyer are not available/traceable.
 - 4. goods have either been destroyed or auctioned by the port authorities at the destination due to non-delivery of goods or non-payment of taxes, etc.
 - 5. legal action is very expensive with reference to the amount to be recovered.
 - 6. exporters surrender proportionate incentives, if any, received from Government of India (duty drawbacks) or any other agencies.
 - 7. submits a certificate from a Chartered Accountant certifying the export realizations during the preceding calendar year.
- c. The exporter can “self-write-off” up to 5%, and Status holder exporters up to 10% and authorized dealer up to 10% of the total export proceeds realized during the previous calendar year.

Consignment Exports

- a. When consignment exports are made, the account sales submitted by the exporter as received from his agents should be verified by the Authorised Dealer.
- b. In consignment exports, the freight for exports and marine insurance should be arranged before exports in India.
- c. In case consign export relates to books, unsold books may be abandoned in foreign country and the value thereof should be shown as deduction from export proceeds of books.

Shipments Lost in Transit

When shipments from India for which payment has not been received either by negotiation of bills under letters of credit or otherwise are lost in transit, the AD Category – I bank must ensure that insurance claim is made as soon as the loss is known.

Netting of Export Receivables Against Import Payments

- a. Requests received from exporters for netting off export receivables against import payments for units located in SEZ are allowed by Authorized Dealer subject to:
 1. The 'netting off' of export receivables against import payments is in respect of the same Indian entity and the overseas buyer/supplier (bilateral netting) and the netting may be done as on the date of balance sheet of the unit in SEZ.
 2. The details of export of goods are documented in EDF (O) forms/ DTR while details of import of goods / services are recorded through A1/ A2 form. The relative EDF will be treated as complete by the designated AD Category – I bank only after the entire proceeds are adjusted/ received.
 3. Both the transactions of sale and purchase in 'R' - Returns under FET-ERS are reported separately.
 4. The export/ import transactions with ACU countries are kept outside the arrangement.
 5. All the relevant documents are submitted to the concerned AD Category – I bank who should comply with all the regulatory requirements relating to the transactions.

Short Shipments and Shut out Shipments

- a. When part of a shipment covered by an EDF already filed with Customs is short-shipped, the exporter must give notice of short-shipment to the Customs.
- b. Where a shipment has been entirely shut out and there is delay in planning to re-ship, the exporter will give notice in duplicate to the Customs in the form and manner prescribed, attaching thereto the unused duplicate copy of EDF and the shipping bill.

Other Conditions in Exports

The following are other conditions in exports:

- a. AD Category – I bank may allow payment of commission, either by remittance or by deduction from invoice value, on application submitted by the exporter.
- b. AD Category – I bank, through whom the export proceeds were originally realized may consider requests for refund of export proceeds of goods exported from India and being re-imported into India on account of poor quality.
- c. Reduction in invoice value on account of prepayment of usance bills permitted up to proportionate interest on the unexpired period of usance calculated at interest rate LIBOR.
- d. Reduction in invoices in other cases such as consignee demanding reduction before making the payment will be allowed by the Authorized Dealer up to a reduction not to exceed 25% of invoice value, the export commodities are subject to floor price, the exporter is not RBI caution list and incentives if received are surrendered.
- e. Change in buyer or consignee are also allowed by Authorized Dealer.

The Key points relating to various guidelines issued by RBI on Imports are narrated below:

- (i) Export Trade is regulated by the DGFT under the Ministry of Commerce & Industry. While the physical merchandize, concept is governed by the Foreign Trade Policy and implemented by the Customs Authorities, the foreign exchange part is governed under the FEMA regulations and implemented by the RBI through the Authorized Dealers.
- (ii) AD Banks should ensure that the Exports from India are in conformity with the FTP in force (2009-14), FEMA rules 2000, adherence to the provisions of statutory guideline, wherever applicable & directions by RBI from time to time.
- (iii) AD Banks should ensure normal banking procedures; KYC guidelines & adhere to the provisions of the UCP while advising/negotiating under LCs for Exports from India.
- (iv) Where specific regulations do not exist, AD Banks may be governed by normal trade practices in all their dealings.

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- (v) All Export contracts and invoices shall be denominated either in freely convertible currency or in Indian rupees. However, exports realized in rupees should be through a freely convertible Vostro account of a non-resident Bank situated in any country, other than a member country of the ACU or Nepal or Bhutan.
- (vi) Advance Remittances towards Exports - Exporters are permitted to receive Advance remittances towards Exports subject to the condition that the shipment of the goods should be affected within one year from the date of receipt of advance remittance. In case if the Exporter is unable to ship the goods within one year from the date of receipt of the remittance, any extension for shipment of the goods or for refunding the amount after one year requires prior approval from the Reserve Bank of India.
- (vii) The amount representing full value of export value of goods shall be received through an AD Bank either in the form of Currency Notes, Bank Drafts, Pay Order, Banker's cheque, debit to FCNR/NRE account or through International Credit Cards of the Buyer. Exports realized in the form of Currency Notes tendered by the Overseas buyer during the personal visit to India can be accepted subject to the obtention of Currency Declaration Form (CDF) where the proceeds exceed USD 5000 and after exercising due diligence as per AML guidelines.
- (viii) All exports are to be supported by the original commercial/financial documents and accompanied by the Exchange Control Copy of the SDF/GR/SOFTEX/PP forms.
- (ix) It is obligatory on the part of the exporter to realize and repatriate the full value of goods or software to India within a period of 9 months from the date of export irrespective whether the Exporter is a status holder exporter or a 100 % EOU. However, in case of SEZs, there is no specific time stipulated for realization and repatriation of the export proceeds.
- (x) EEFC – Exchange Earners Foreign Currency Accounts may be opened by Exporters to park the exchange earnings realized on account of exports to the extent of entire 100 % of the proceeds. However, exporters are under obligation to convert the entire balances into rupees before the last day of the next calendar month after utilizing the

balances for import payments, if any and against forward contracts booked against the balances.

- (xi) General permission is available to all Exporters for opening of a temporary foreign currency account for participation in trade fairs and exhibitions abroad. Exporters are permitted to export goods for the purpose of exhibiting the same in overseas exhibitions, sale of goods in such exhibitions and repatriating the sale proceeds on conclusion of the exhibition. Exporters are also permitted to re-import the goods into the country after completion of the exhibition.
- (xii) Unrealized Export Bills – Exporters have to follow-up with the overseas buyers for realization of the Export bills and repatriation of the proceeds thereon. However, due to the reasons beyond the control of the Exporter, if the goods exported are not realized within the due dates, the Exporters can get the export bills extended by submitting Form ETX along with the copies of documents evidencing follow-up with the overseas buyers. AD Banks will take on record the efforts put in by the Exporter and extend the due date for realization of the bills accordingly. Despite efforts by the Exporter for realization of the Exports, such bills can be written off by the Exporter either by Self-write off or write off by the AD Bank in their books subject to adhering to the extant guidelines of RBI.

Foreign Contributions

Foreign contributions received in the country for person resident in India are governed by Foreign Contribution (Regulation) Act, 2010 read with Foreign Contribution (Regulation) Rules, 2011.

The Act is applicable to whole of India and to foreign branches and subsidiaries of “Body Corporates registered in India”. However, the act is not applicable to a company registered under the Companies Act whose more than half of nominal capital is held by a foreign company or foreign source.

Foreign Source

Foreign source includes:

- (i) The government of any foreign ‘country’ or ‘territory’ and its agency(s).
- (ii) Any international agency (not being the United Nations or any of its specialized agencies).

- (iii) a foreign company.
- (iv) a corporation, not being a foreign company, incorporated in a foreign country or territory.
- (v) a multi-national corporation as per clause (g).
- (iv) A company within the meaning of the Companies Act, **2013** and more than one-half of the nominal value of its share capital is held, either singly or in the aggregate by certain agencies mentioned in the Act.
- (vi) A citizen of a foreign country.

Foreign Contribution

Foreign contribution (FC) means the donation, delivery or transfer made by any foreign source of any:

- (i) Article, (not being an article given to a person for his personal use as a gift having market value of not more than 25,000) (present specified threshold).
- (ii) Currency (includes Indian or foreign).
- (iii) Security (per Section 2(h) of the SCRA, 1956 and includes any foreign security per Section 2(o) of the FEMA, 1999).

Cost in lieu of goods or services in the ordinary course of his business, trade or commerce shall not be treated as FC. However, the infusion of foreign share capital in a company registered under Section 25/ Section 8 of the Companies is treated as FC.

Recipients of Foreign Contribution

Who can receive

Any Person who is having a definite cultural, economic, educational, religious or social programme (practically all NGO's having nationalist objects) can receive FC after getting registered under FCRA law or obtaining a prior permission from the Central Government. A private limited company may also seek prior permission/registration for receiving foreign funds in case they wish to do some charitable work.

Who cannot receive

In terms of Section 3 of the Act, foreign contribution shall not be accepted by the following persons:

- (a) A candidate for election.
- (b) Correspondent, columnist, cartoonist, editor, owner, printer or publisher of a registered newspaper.
- (c) Judge, government servant or employee of any corporation or any other body controlled by Government.
- (d) Member of any legislature.
- (e) A political party or officer bearer thereof.
- (f) Organization of a political nature.
- (g) Association or Company engaged in production or broad cast of news.
- (h) Prohibited individuals or Associations.

In terms of Section 4 of the Act, foreign contribution can be accepted by:

1. Relative. (Any person receiving FC more than one lakh rupees or equivalent thereto in a financial year from any of his relatives shall inform the Central Government in Form FC-1 within thirty days from the date of receipt of such contribution.
2. Business receipt from official channel or as per FEMA, 1999.
3. Scholarships.
4. Wages for employees working under him.
5. As an agent of foreign of source for transactions with CG/SG.
 - a. No permission is required from Central Government if foreign contribution is accepted in the form of:
 1. Salary, wages, or other remuneration due to him.
 2. By way of payment during international trade or commerce.
 3. As an agent of a foreign source.
 4. By way of gift or presentation made to him as a member of any Indian delegation.
 5. By way of any scholarship, stipend, etc.
 6. Receipt of contribution from a relative not exceeding USD 8000 per annum.

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7. Remittance received in ordinary courses of business through official channels.
- b. The person accepting foreign contribution in the aforesaid manner needs to register with the Ministry of Home Affairs and obtain a certificate of registration as specified under the Act.
- c. They should also get the accounts audited periodically and submit the reports to the Government.
- d. They must designate a Bank's Branch for receipt of contributions.
- e. A person receiving scholarship, stipend will intimate Central Government if such amount exceeds USD 36000 in an academic year.
- f. Donations accepted from an Indian who has acquired foreign citizenship, PIO/OCI card holders are treated as foreign contributions. However, contributions received from non-resident Indians need not be reported.

Role of Banks

- a. Bank should send a report to Central Govt. within 30 days where an amount more than Rs. one Crore has been received in the case of registered entities and in the case non-registered entities, any amount received thereof.
- b. Bank should not allow any withdrawal or transfer or utilization of the FC amount till such time the Association produces documentary evidence from MHA permitting it to do so.
- c. FC that is returned to the donor (for want of registration or prior permission) without crediting in the account of the recipient need not be reported.
- d. Transfer of funds from one FCRA registered Association to another need to be reported.

Other Important Areas of Foreign Exchange

1. Foreign Current Asset (FCA):
 - a. FCA is a debt instrument issued by another country.

- b. Every country wants to invest Foreign Exchange (FE) in that FCA, to gain the profit at the time of realization of FCA.
 - c. FCA can be made in the form of Dollars, Yen, Euro and Pound.
- 2. Balance of Payments:
 - a. If import exceeds Export, India will have Less FE, which will show “adverse” payments position.
 - b. If Export exceeds Import, India will have More FE, which will show “Favourable” Payment’s position.
- 3. Inflow of FE comes from:
 - a. FDI/FII/FPI (foreign portfolio investment).
 - b. Exports.
 - c. Loans borrowed/ Loan returned.
 - d. NRI remittance.
 - e. Permanent return of NRI.
 - f. Capital Account transactions.
 - g. Current account transactions.
 - h. Investment in Government projects.
 - i. Realisation of FCA.
 - j. Government securities.
- 4. Outflow of FE goes from:
 - a. Taken back by FDI/FII.
 - b. Imports.
 - c. Loan repayment/ Loan given.
 - d. Payment towards FCA.
 - e. LRS.
 - f. Capital Account transactions.
 - g. Current Account Transactions.
 - h. Investment in Foreign Government Projects.

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5. Foreign Exchange Highlights:
 - a. Each country wants to deal with its own sets of rules and regulations and in its currency.
 - b. Currency differs from country to country.
 - c. Every Indian wants to save their money only in Indian Rupee and not any other Country's currency.
 - d. All the Exporters want the money in their country's currency.
 - e. When one Country's currency is converted into another country's currency, then it is called as Foreign Exchange.
 - f. In India Authorised Dealers/Banks are responsible for Conversion of currency.
6. FE is dealt by the following authorities in India:
 - a. Reserve Bank of India (RBI).
 - b. Director General of Foreign Trade (DGFT).
 - c. Authorised Dealers (AD).
 - d. Foreign Exchange Dealers Association of India (FEDAI).
7. Authorised Dealers: (AD)
 - a. Authorised Dealers are appointed by RBI, to do Limited / Unlimited dealings in FE in India.
 - b. Licence of AD may be cancelled/revoked/refused by RBI.
 - c. AD must according to the powers given by RBI.
 - d. In case AD has acted Outside powers, then AD must refer to RBI.
8. FE requirement and usage:
 - A. FE is required for AD/ Customers.
 - B. FE is purchased/sold by AD/ Customers.
 - C. FE is required to be bought and sold by AD to earn profit.
 - D. FE is required to be bought and sold by the customer to meet their requirements.
9. Mode of operation of FE:

A. AD buys FE in Discount from Public/ Interbank/ Other Countries.

B. AD sells FE at Premium to Public/ Interbank/ Other countries.

10. Highlights of FEMA, 1999:

a. Foreign Exchange Management Act, 1999 has become effective from 1/6/2000 in India.

b. RBI is the Overall controlling Authority of FEMA, 1999.

c. Central Government makes rules under FEMA, 1999.

d. FEMA, 1999 extends to whole of India.

e. FEMA, 1999 Applies to all branches, offices and agencies situated in India.

f. In case if branches, offices and agencies situated outside India and is controlled by a person resident in India, then FEMA 1999 is applicable.

g. Hence if any contravention is committed person as stated by Para 10(f), then they are also under the control of RBI.

11. Foreign Currency Accounts:

The following are the Foreign Currency Accounts.

1. Nostro Account.

2. Vostro Account.

3. Loro Account.

12. Nostro Account:

a. It is an opened by Any bank in India at the Foreign Country.

b. This account is opened in foreign country in that country's currency.

c. This account can be used towards Receiving Export Proceeds.

13. Vostro Account:

a. It is an account opened by any Foreign Banks in India in Indian Rupee.

b. This account can be used towards sending the Import proceeds.

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14. Loro Account:
 - a. Indian Banker quotes another Banks account.
 - b. Through this account transactions can be carried out for Export proceeds or import proceeds, though the account opening bank is not having any account in another country.
15. Foreign Exchange Transactions:
 - a. FE dealing in foreign currency is called as "Commodity".
 - b. In India FE is not a legal tender.
 - c. Debt in India cannot be settled in FE.
 - d. In India Only AD including banks are authorized to carryout FE.
 - e. There are Two Quotes in FE:
 1. Direct Quote: Where Indian Rupee value is constant and FC value is fluctuating.
 2. Indirect Quote: Where Foreign Currency value is constant, and INR is fluctuating.

PART III

Concurrent Audit Checklist and Core Banking System

Chapter 1

Concurrent Audit Checklist

For effective concurrent audit, it is essential that the audit planning and Audit programme are detailed and pre-planned. The Transactions are numerous, and all those transactions must be verified within the prescribed time given by the Bank's Head Office to the Concurrent Auditor. For audit, the Concurrent auditor must plan his schedule of work by way of proper planning. The Checklist proposed here is suggestive in nature. The concurrent auditor may carry out the audit based on his Audit Programme and Audit Plan within the given time limit. In Concurrent audit, Time Planning is important for a meaningful audit.

This checklist is based on suggested item of coverage as per RBI Circular "*Concurrent Audit System in Commercial Banks – Revision of RBI's Guidelines*" dated July 16, 2015, and its subsequent circulars.

Unless there is a specific guideline by the bank, the suggestive checklist of various items with periodicity is given below:

(A) Cash

Physical Verification of Cash:

- Verify Opening Cash that has been kept under lock and key physically and see that the same is tallied with Cash Vault Register. For this the audit team should go to the branch before opening the Cash vault.
- Alternatively, Verify Closing Cash physically after the day end before the Cash has been kept inside the vault and see that the same is tallied with Cash Vault Register. The audit team must check the Cash Counter (closure entries) Register also.
- In the Concurrent audit, as per the Appointment letter, auditor can also ask the Branch Manager to stop the "Counter Cash" transactions to do surprise Check, at least once in a Quarter (but it depends on the terms and conditions of appointment letter). When the auditor has planned to do this "Counter Cash" verification, the Branch must open an Additional Cash Counter with the intention of carrying the daily cash transactions without any interruption.

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- Physical verification of Cash at Branch and Cash in ATM and its reconciliation with GL to be checked.
- Cash includes:
 - a. Indian Rupee and Coin.
 - b. Foreign Currency and Coins.
- Auditor must verify whether the branch has followed the “Clean Note Policy” of RBI. i.e. No cash bundles are stitched/ stapled.

Auditor should ensure that the branch is equipped ultraviolet UV machine for detecting counterfeits, note sorting machine and note counting machine and that they are in use.

- Auditor must Verify ATM Cash (wherever is the ATM located) and compare the same with ATM Cash Ledger Folio and satisfy that there is no difference. In case of any difference, the Auditor must ask the Branch Manager to do the reconciliation of difference. It is to be noted that the reconciliation must be done only by the Branch and not by the auditor. The auditor role is only to verify the reconciliation statement.
- ***Check following registers for ATM:***
 - 1. Customer Complaint Register.
 - 2. ATM Problem Register.
 - 3. ATM Cash Deposit /Replenishment Register.
 - 4. ATM Card Issue Register.
 - 5. ATM Pin mailer issue Register.
 - 6. PIN regeneration Request Register.
 - 7. ATM Key Register.
 - 8. ATM preventive Maintenance File.

Other areas of Cash verification: (In case of any difference/ violation/ deviation the same must be reported the Auditor in detail with evidence:

1. Verify Daily Cash Transactions with the Cash Report Generated from the system at the day end and the auditor must authenticate that report.

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2. In case there are any abnormal receipts and payments, the auditor must verify those entries and report from PMLA activity, if any
3. Verify the Cash Bundle Vouchers daily, after the same is checked and certified by the Branch Officials.
4. The periodic of verification of Cash Bundle (whether daily or weekly) is clearly mentioned in the Appointment Letter.
5. Verify whether Cash vouchers have been properly verified and passed by the officers.
6. Surprise Check at the Cash vault "Cash" has to be done by the following persons, other than Key Holding persons. (As per HO directives):
 - (a) Branch Manager (once in a Month).
 - (b) Other Branch Staff (once in Quarter).
7. Verify when the cash transactions exceed Rs. 50000/, PAN is quoted by the Customer. The auditor must see whether PAN details have been recorded in the system and if they are there, there is no need to mention PAN details in the voucher, even if the amount exceeds Rs. 50000.
8. Verify all cash inward Transactions (cumulative) more than Rs. 10 lakhs (Per Financial year) have been reported in CTR. This applies to remittances in Savings account / Current Account / Deposit accounts.
9. Verify all Cash Expenses transactions with Cash register including Petty cash register and see whether Capital expenditures have been included in the Revenue Expenditures.
10. No cash payment is allowed in the case of Bearer Cheque payments/ DD Payments if the value is Rs. 20000 and above.
11. In the case of Deposits (matured or not) repayment along with interest is Rs. 20000/- no cash payment is allowed and the same has been given credit to SB/CA of the Customer.
12. Auditor must ask for the Cash Retention Letter and do the Audit with Cash Stock register to ascertain the days on which the Cash Retention Limits have exceeded. And the auditor must see whether the same has been reported to the Controlling authorities by the branch.

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13. Auditor must ask for Cash insurance policy and see the terms and conditions stated in the policy.
14. Auditor must verify the Cash In transit register and ascertain the following:
 - a. See the amount of cash transited as per the Controlling authorities' directions.
 - b. Who has carried the cash during the cash in transit and whether that officer has put his consent of carrying the cash in the register.
 - c. The date and time of remittance of cash at the other branch/Chest branch/other banks.
 - d. The acknowledgment of Cash receipts duly signed by the officials of other branch/chest branch/ other banks.
 - e. In case the cash is remitted beyond 6 pm in the evening, the reason for late remittance to be seen.
 - f. Proper security care is being taken during the Cash in transit by the branch.
15. A separate register for the Counterfeit notes must be kept with the following details:
 - a. Name of the customer who has remitted the counterfeit notes.
 - b. Name of the Officer/cashier who has detected the counterfeit notes.
 - c. Date of occurrence of the detection.
 - d. Reporting to Controlling authorities about the incidence.
 - e. Reporting to the Police by way of complaint as per the direction of RO/ZO/HO.
 - f. Reply submitted by the Customer who has remitted counterfeit notes.
16. Verify all the Currency Chest remittances/receipts by the branch and the acknowledgement with reference to the transactions.
17. Verify all the reports submitted to RBI with reference to currency chest transactions.

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18. Auditor must verify that the Duplicate keys of Cash vault (strong room), and almirah are kept under the Joint custody of the officials of the Branch.
19. In case the branch is holding foreign currency / coins, the same must be approved by HO/ZO/RO. The auditor must verify the Authorisation letter issued by HO/ZO/RO with reference to holding of foreign currency.
20. Auditor must verify the Token register and see that "lost Token" details have been recorded in the ledger as well as proper display in front of Counter Cash Cabin.
21. Auditor must verify Cash Excess/Short register and analyse the reasons and report.
22. Auditor must verify the Cash Fraudulent transactions that took place in the form Misappropriation / Theft at the branch and report the latest status of those types of transactions.
23. Auditor must prepare a separate Cash Check List Programme before commencement of the Cash Verification.

(B) Clearing

- (i) Whether drawings are allowed against uncleared instruments.
- (ii) Whether such instruments are referred through prescribed register and passed by the Controlling Officer, if the drawings exceed the prescribed limit whether these are reported to the Controlling Authority.
- (iii) Examine whether interest was charged and report such omission for rectification.
- (iv) Verify whether:
 - Proper accounting of inward and outward clearing is being done on daily basis.
 - Safeguards are observed to ensure proper handling and custody including returned instruments.
 - Service charges/incidental charges as prescribed are charged for the cheques returned in clearing.
- (v) Verify whether credit for realized cheques is received promptly.

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- (vi) Whether settlement is on daily basis? And that MO of outstanding entries, if any is prepared?
- (vii) Whether the system of Positive Pay has been implemented and the acknowledgements by the customers are preserved?

(C) Remittances/Bills for Collection – Inward and Outward

- (i) Verify remittance of funds by way of NEFT/ RTGS or any other mode in cash is exceeding the prescribed limit.
- (ii) Verify documents of title (lorry receipts, railway receipts, etc.) obtained in favour of the bank and confirm that the concerned transporters are on the IBA approved list.
- (iii) In case the branch is holding the Title receipts of Transporters who are not in IBA approved list, the same must be verified by the auditor from realization and risk concept.
- (iv) Verify whether proper accounting of inward and outward remittance transactions is done.
- (v) Outstanding balance in DP and other transit accounts pending payment beyond prescribed period and the steps taken by the bank to recover the same.
- (vi) Verify whether prescribed service charges by way of exchange, commission, out of pocket expenses, interest, overdue interest in respect of all remittances, bills purchased, and collection items are recovered.
- (vii) Verify whether branch detains inward bills/ cheques/ collection item beyond the stipulated period.
- (viii) Verify physically the inward bills on hand and post parcels tally with records.
- (ix) Verify whether returned bills are debited to "Past Due and Dishonoured Bills" and followed up as per the guidelines.
- (x) Verify whether overdue bills are properly followed up/ non-payment notices are served.

Demand Draft/ Pay Order

- (i) Verify whether DDs/ PO of 50,000/- and above are issued through

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accounts and not against cash.

- (ii) Verify whether DD/ PO issue charges have been collected as per the Service charges circular of Bank.
- (iii) Verify the Number of DDs/ PO issued on payment of cash basis, particularly @ Rs.49,000 daily on receipt of cash and without quoting PAN.
- (iv) Verify the security items of unissued DD/ PO on hand and see that it tallied with the stock register.
- (v) Verify the cancellation of DD/PO and see that the credit is being given credit to customer SB/CA on production of "counterfoil" of DD/ PO application.
- (vi) As an auditor, the purpose of cancellation of DD/ PO has to be verified from the genuineness and if not there will be lot of scope for Fraudulent transactions or encashment of stolen DD/ PO from the beneficiaries after the purpose fulfilled (e.g. after getting license renewed, the government staff would have removed the same from the file without sending the same for collection etc).

(D) Deposits

- (i) Verify adherence to KYC/ AML guidelines in opening of fresh accounts and monitoring of transactions in such accounts and whether letter of thanks is being sent to new depositors. It would be advisable to also cross verify with the postage expenses and the outward register.
- (ii)
- (iii) Verify whether Form No. 60 where the depositor does not have PAN is held on record and the same are submitted as per laid down procedure.
- (iv) Verify large term deposits received and repaid including checking of repayment of term deposit in cash beyond permissible limit.
- (v) Verify accounts opened and closed within a short span of time, i.e., accounts with quick mortality.
- (vi) Verify whether the receipt/ payment of term deposit beyond Rs. 20, 000/- is made only through current/savings bank account. or by A/c payee cheque.
- (vii) Verify that inoperative/ dormant accounts are properly flagged, and

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separate control thereon is exercised. Operation in dormant accounts is authenticated by the competent authority. Concurrent auditor shall verify the last transaction date in such accounts.

- (viii) Verify value dated transactions.
- (ix) Verify renewal procedure of term deposits. Whether deposits are auto renewed on due date if not closed.
- (x) Verify Interest paid on deposits during the quarter ended March, June, September and December, respectively as to whether the interest is correctly paid and maturity values correctly calculated at the prescribed rates as applicable to the category and term of deposits.
- (xi) Verify the working of Pre closed Deposits, particularly TDS payments are made against those deposits.
- (xii) Verify whether the Nominee clause is properly entered in the Deposit account.
- (xiii) Verify the records of Form 15G/ Form 15H submitted to the bankers as per the Bank's HO directions.
- (xiv) Verify that deduction of tax at source from interest income on term deposits is made as per laid down procedure.
- (xv) Verify procedure in place for settlement of claims of deceased customers and payment of TDRs against lost receipts and obtention of indemnities, etc.
- (xvi) Verify revival of dormant accounts and accounts with minimum activities.
- (xvii) Examination of multiple credits to single accounts.
- (xviii) Verify whether service charges for the return of cheques, issue of cheque books, carrying out standing instructions and minimum balance charges are levied as per prescribed norm.
- (xix) Scrutiny of staff accounts to detect any abnormal transaction.
- (xx) Verifying that stop payment instructions are being recorded properly.
- (xxi) Specific checks w.r.t debits in the inoperative accounts.
- (xxii) Shifting of inoperative/ dormant account to operative account is to be backed with KYC norms. Check the procedure for preservation and

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update of KYC records in respect of revived accounts.

- (xxiii) Cash withdrawal in dormant account should be done personally by the account holder.

Account Opening Procedure

- (i) These are filled in all respects and KYC norms are complied with. Verify system-generated alerts for KYC refreshes. Ensure high-risk customers have undergone timely refresh as per RBI mandate. Banks are now to obtain C-KYC. Check the process of obtention of CKYC and for follow up of pending accounts.
- (ii) Photostat copies of all documents/ papers attached to the account opening forms are verified from the original and the bank official has passed necessary remarks with his signature on the Photostat copies for having verified the same for original.
- (iii) Latest Photographs of the depositors/ all the authorized signatories are obtained and other requirements such as introduction, date of birth certificate in case of minors, nominations, etc. are complied with.
- (iv) Round stamp of the bank is affixed on photographs. Name of depositors is written on the reverse of the photographs.
- (v) The bank officials must verify the Bonafide of the depositors and introducers, if required.

Debit Balance in Saving and Current Account

- (i) Un-recovered debit balances in savings and current account that might have arisen due to various reasons are reported.
- (ii) Interest on such debit balances is promptly recovered.

Issue of Cheque Books

- (i) Proper procedures are followed for issuing of cheque books.
- (ii) In case of Cheque books delivered to third person, necessary precautions as mentioned below are taken.
 - (a) Authority letter bearing an attestation of signature of the person who is authorized to collect the cheque book, by the customer should be obtained.
 - (b) Customer signature of said letter should be verified by the bank official.

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- (c) Identity of the receiver of the Cheque book is established.
- (d) Cheque book receiver's signature is taken on the cheque book issued register.
- (e) Account holder is informed accordingly through SMS on mobile wherever possible.
- (iii) Cheque books prepared but not delivered to the customer are kept safely under lock and key with the officer.
- (iv) Guidelines as indicated in circulars issued from time to time regarding disposal of undelivered cheque books are followed.
- (v) Wherever applicable, charges are received.
- (vi) Cheque book when issued is immediately authorized in the system.

Nominations

- (i) The appropriate nomination forms for deposits, lockers and safe custody are obtained and are serially numbered.
- (ii) Nomination is entered in the system and authorized immediately.
- (iii) The signature of the customer making the nomination is verified. Date of receipt of the nomination is marked on the nomination form/ account opening form.
- (iv) Necessary remarks are noted on account opening forms, in the computer system and register.
- (v) Screen print of nomination is attached to the application forms/ account opening form.
- (vi) Acknowledgement of having received and registered the nomination is issued to the customer.
- (vii) Nomination Register is maintained properly and posted up to date.
- (viii) In case of settlement of claims to nominee, proper procedure is followed. KYC proofs as per the RBI guidelines of the nominee are obtained. Date of registration of nomination and the date of death of the depositor should be checked while settling the death claim to the nominee. In case of request from the depositor the term deposit receipt wise nomination be accepted.

However, while accepting the receipt wise nomination or account wise nomination in case of term deposit the following clause be inserted in the nomination form. "Nomination given in the nomination form for the receipt/s or term deposit account will be continued even after the renewal of the said term deposit/s unless the contrary fresh nomination instructions in the fresh nomination form are submitted to the bank."

Death Claim

- (i) All death claims are settled within a fortnight.
- (ii) The claim form is duly filled in.
- (iii) NOC from all co-heirs, "Affidavit" on stamp paper regarding legal heirs duly notarized and signed by guarantors, etc. is obtained.
- (iv) The claim has been sanctioned, and documentation has been done accordingly.
- (v) Death Certificate of the Borrower must be produced.
- (vi) As per the amendment in BR Act, 1949 (amendment in 2024) – death claims are to be settled on the nominees.

(E) Treasury Operations

- (i) Verify if branch has acted within HO instructions for purchase and sale of securities.
- (ii) Periodic confirmation of derivative contracts with counterparties has been obtained.
- (iii) Adherence to regulatory guidelines with respect to treasury deals/ structured deals.
- (iv) Controls around deal modification/ cancellation/ deletion, wherever applicable.
- (v) Cancellation of forward contracts and passing/ recovery of exchange gain/ loss.
- (vi) Gaps and OPL maintained in different currencies vis-à-vis prescribed limit for the same.
- (vii) Reconciliation of Nostro and Vostro accounts-balances in Nostro accounts in different foreign currencies are within the limits prescribed by the bank.

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- (viii) Collection of underlying documents for derivative and forward contracts, delays, if any.
- (ix) Instances of booking and cancellation of forward contracts with the same counterparty within a span of couple of days or a few days.
- (x) Sample check some of the deals and comment on the correctness of computation.
- (xi) Checking of application money, reconciliation of SGL account, compliance to RBI norms.
- (xii) Checking of custody of unused BR forms and their utilization in terms of Master Circular on Prudential Norms on Classification, Valuation and Operations of Investment Portfolio by banks.
- (xiii) To ensure that the treasury operations of the bank have been conducted in accordance with the instructions issued by the RBI from time to time.

(F) Advances

Application & other documents (new / additional loan / renewals)

Application form has been submitted, duly complete in all respects, in the format prescribed by the Bank, along with necessary supporting documents such as KYC/ Identity Proof Documents (Aadhaar, PAN, Voter ID, Passport), Address & age proof documents.

To ensure that KYC documents have been verified online from the respective websites.

Applicant/ Borrower has submitted copies of audited financial statements, Tax Audit Report, Income tax returns, GST Returns, Project Reports, etc. at the time of fresh application/ Renewal/ review of accounts. (11) Branch has confirmed the UDIN on audit reports from the ICAI website. Income Tax & GST documents have been confirmed from the concerned websites.

Credit Appraisal

Credit appraisal of the proposal has been properly carried out, as per the norms prescribed in the credit policy of the Bank and Credit Appraisal Note captures all critical items.

Credit Proposal is disposed within the prescribed time norms with

emphasis on credit sanction efficacy at branch level.

Pre-sanction inspection to the registered address of residence/ workplace/ business place of borrower is conducted by the Bank's officials and properly documented.

Internal credit rating prepared by the Bank should be verified to ensure that the same is based on the norms prescribed by the Bank. Report of external credit rating is obtained, as per the bank's policy.

Credit Score of the borrower/ Partners is verified by the Branch. The CIBIL/ CRIF/ CRILIC report on borrowers generated from the respective platform is kept on record.

The Central Fraud Registry website has been verified, if required, as per the bank's guidelines.

CERSAI website is verified during appraisal of the loan and details are kept with the loan document with CERSAI registration papers.

Assets & Liabilities statement obtained from the borrower(s)/ Directors/ Partners/ Guarantor(s) are properly scrutinised for commitments of other loan repayments.

Credit Sanction

Auditor should go through the Sanction Letter carefully to verify the following aspects.

Verify fresh advances (including staff advances) have been sanctioned properly, in compliance with credit policy/ procedures of the bank and in accordance with delegated authority. In case delegated authority is exceeded, ratification in writing from appropriate higher authority is obtained.

Loans are sanctioned as per the credit policy of the bank and adhere to the regulatory (RBI) norms unless a specific exemption is taken in this regard.

Whether all terms and conditions as specified in sanction letter have been complied with and to ensure "Certificate of Compliance" if any of sanction terms are submitted to respective sanctioning authority. In case particular condition is not complied, time extension for the same is obtained from appropriate higher authority.

Documentation

Verify whether securities and documents have been received as applicable to loan.

Whether Legal Vetting Certificate, wherever prescribed had been taken.

Verify master data relating to limit, rate of interest, EMI, moratorium period details have been correctly entered and updated/ modified in the system.

Ensure that Proper Documents have been obtained properly as per HO Directives.

Ensure that the branch is in possession of all the Documents dealt/ mentioned in the Legal Opinion.

Ensure that Key Facts Statement (KFS) is issued to the borrower, as per the directives of the RBI.

Proper Updating of Master Data in CBS

Concurrent Auditor should verify that master data of the borrower has been properly updated in CBS after first time entry and after modifications, if any. Various details should be verified, such as:

- KYC particulars.
- Contact Details of borrower(s) such as Mobile Number, e-Mail IDs, address etc.,
- Loan scheme code.
- Priority sector / other sectoral classification.
- Amount sanctioned.
- Rate of Interest.
- Repayment schedule.
- Interest payment date.
- Moratorium period.
- Amount of Instalment/ EMI.

Auditors should ensure that rate of interest in master data of CBS is changed after each change in MCLR of the bank.

Disbursement/ Operations in account

Verify that disbursals are allowed against proper sanction, within sanctioned limits and drawing power.

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Verify that disbursement in term loan account is directly made to the suppliers / vendors and proper documents of utilisation (such as copies of invoices/ receipts) are obtained on record.

In respect of medium/ large advances, utilisation certificates from chartered accountants are obtained on monthly/ periodically as specified in the sanction letter. Also, wherever specified monitoring of the project under construction is carried out by lenders' independent engineer (LIE) and disbursement is made as per his recommendations.

Verify reporting of instances of exceeding delegated powers to the controlling/head office by the branch have been confirmed or ratified by the competent authority.

Verify operations allowed in advances accounts:

- Whether they are within the sanctioned limits of drawing power (worked out as per the latest statements and prescribed margin).
- Whether operations in the accounts reveal any unhealthy features, such as, heavy withdrawals in cash suggestive of diversion of funds for purposes other than the declared business of the borrowers, diversion to sister/ associate concerns, diversion of funds to other banks (which are not members of the consortium), kite flying, etc., or any other sticky/ unhealthy tendencies which may jeopardize the interest of the bank.

Verify value dated entries passed in advances accounts.

Comment on the turnover in the cash credit account and significant variations between the turnover reported as per financial statements and magnitude of transactions put through bank account.

In case of consortium accounts, details of turnover in working capital limits are shared with all the member banks and the turnover in accounts with all the banks is in line with the sales turnover / revenue of the borrower.

Drawing Power

Verify whether in the case of all advances against hypothecation of goods/ stock/ book debts, etc. [CC (hypothecation), PCL (hypothecation), etc.]

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- Periodical statements declaring stock/ debtors, etc. as the case may be, are received from the borrowers within the stipulated due dates, whether the statements are properly scrutinized by the branch officials.
- Reports of verification of securities by third parties are received timely and whether penal charges are being charged for delayed submission. Reports are as per requirements of respective banks.

Verify whether book debt statement certified by a chartered accountant, as stipulated by the bank, has been obtained.

Verify whether creditors have been reduced while calculating DP.

Verify whether monthly updating of drawing power in the computer system based on stock statements/book debt statement/ other financial data has been received from the borrowers.

Verify if stock statements (indicating the location) are being received at stipulated intervals, the statements are properly scrutinized, drawing power is correctly calculated, DP Register is maintained and drawings/ availments in the account so regulated. If the stock is with third party, then obtain NOC from the third party and their bankers.

Ensure obtention of Certificate of Chartered Accountants prescribed for Debtors ageing and Debtors balances should be verified.

Ensure that stock audit is conducted as per the terms of sanction and also in all eligible accounts as per bank's policy. The stock audit report should be verified and explanations furnished by the borrower on discrepancies pointed out in the stock audit report should be reviewed and commented, if required.

Interest & charges

Ensure that interest is debited to the loan/ cash credit account accurately, including penal interest on overdue, excess drawings, late submission of financial/ operational data / stock statements etc.

Ensure that all charges, such as processing charges, CIBIL charges, documentation charges, inspection charges, lead bank charges etc. have been collected as per Sanction Letter / policy of the Bank.

Security & Charge creation

Verify whether charge on securities have been properly created & registered with Registrar of Companies/ Revenue Authorities in case of mortgage of land/ building. Also, valuation report from approved valuer is obtained in appropriate cases.

Ensure end utilisation of loan sanctioned and that assets have been created properly out of loan sanctioned, by inspection of the assets. In case of medium/ large loans, utilisation certificate from Chartered Accountant is obtained, as per bank's policy.

Verify whether lien is marked on fixed deposits pledged as security with the Bank.

Verify whether NSCs/ KVPs against which advance has been allowed have been pledged in favour of the bank and the said lien is marked by the concerned Post Office. Relevant securities are sent to and received back by the registered post/speed post unless specified otherwise. The envelope for NSCs/ KVPs is held on record.

In case of advance against LIC policy, the amount should be allowed only against surrender value and LIC policy in original with assignment is held on record.

Legal compliance & Due diligence

Ensure that the Borrower has got "updated" Business License to do the Business as per the laws of the Country.

Verify whether any case is pending against the borrower before NCLT/ DRT, other legal forums.

Verify whether the case filed before NCLT/ DRT has been ordered and the position of Decreed cases.

Insurance

Auditor should ensure that fixed assets & current assets of the borrower, which are charged to the Bank are properly insured for all the risks. Following aspects should be verified

- a. Valid Period.
- b. Name of the Borrower tallied with the sanction letter.
- c. Location of the unit.

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- d. Adequacy of amount of insurance cover / No underinsurance.
- e. Bankers' Clause.
- f. Assets tallied with the sanction letter.
- g. Coverage of risks.
- h. Timely renewal / maintenance of due date diary.

Credit monitoring

Verify whether credit monitoring i.e. post disbursement supervision and follow-up is carried out properly, in terms of credit monitoring policy of the bank, including monitoring in large borrower accounts.

If Agency for Special Monitoring (ASM) has been appointed for any borrower, the Concurrent Auditor should review discrepancies pointed out in the monthly report of ASM, compliance/ explanations given by the borrower and should suitably comment on the same in his report, as thought fit.

Credit monitoring such as, timely receipt of stock and book debts statement, QIS Data, analysis of financial data submitted by borrower, verification of securities by third parties, renewal of limits, insurance, etc.

Whether Select Operational Data and Management Report/ HMR, where applicable, in respect of big borrowers have been received promptly as prescribed in the sanctioned letter.

Recovery in compromise cases is in accordance with the terms and conditions of the compromise agreement.

Verify (on sample basis) by surprise goods pledged to the bank to ensure that keys of the godown are held in dual custody, goods pledged to the bank tally with the record maintained in the Godown Register and the invoices both for quantity and value.

Verify if godown inspection is being conducted periodically and is properly recorded and reports thereof submitted.

Whether financial performance of the unit is in accord with earlier projections submitted to the bank and included in the appraisal note. Comment on the major variations and explanations received from the

borrower.

To check review / renewal of loans has been done after the due date. Comment on the short reviews sanctioned by the Branch and whether the same are within the policy framework of the Bank.

Comment on the probable diversion of funds and ask the bank to call for explanations from the borrower. Report on the same to the appropriate authorities of the bank, as diversion of funds amount to "Fraud" as per RBI directives.

Repayment/ Credit Defaults

Verify delinquency of loan accounts as per the reports generated from CBS/ system of the bank under SMA-0, SMA-1 & SMA-2 categories and actions taken by the branch for recovery in these accounts.

Verify compliance of prudential norms on income recognition, asset classification and provisioning pertaining to advances.

Whether the branch has issued the SARFAESI notices to the Borrowers on time.

Bills Purchased / Discounted

Verify whether bills are purchased as per terms of sanction and proper margin is maintained as per sanction.

Verify whether pre-sanction verification is done before sanction of BP limits.

Verify and report clean bills/ cheques purchased, if in accommodation bills. Ensure that local cheques are not purchased unless specifically permitted.

Verify proper follow-up of overdue bills purchased/discounted/ negotiated.

ADVANCES – General Highlights

- a. The following Types of Loans have been sanctioned:
 - (i) Funded Advance.
 - (ii) Non-Funded Advance.
- b. Funded Advances have been sanctioned for the following purpose:

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- (i) Term Loan.
- (ii) Cash Credit Loan/ Overdraft Loan.
- (iii) The Term Loans have been sanctioned for the purpose of Domestic Business as well as for Export Business.
- c. Non-Funded Advances have been sanctioned for the following purpose:
 - (i) Issue of Bank Guarantee.
 - (ii) Issue of Letter of Credit.
- d. *LC/ BG*
 - (i) Verify whether issue of LCs/ BGs is in line with the extant guidelines.
 - (ii) Verify whether appropriate commission is collected in respect of fresh/renewed LCs/ BGs.
 - (iii) Whether securities including deposits are linked in CBS to LCs/ BGs.
 - (iv) Verify whether issue of LCs/ BGs is reported timely to Zonal Office/Regional Office.
 - (v) Verify whether LC/ BG is issued/amended as per approved format/model, if any, and whether standard limitation clause is incorporated. Whether counter indemnity obtained as prescribed.
 - (vi) Verify whether there is any deviation from the terms of sanction regarding margin, security, purpose, period, beneficiary, collection of charges, commission, fees, etc.
 - (vii) Whether the branch has paid/ met any guaranteed obligation under bank guarantee issued by it, whether payment is made to the debit of party's account on due date without creating overdraft/ debiting suspense.
 - (viii) Whether bills paid on the previous day under LC are strictly according to terms of the LC; whether reimbursements have been obtained promptly.
 - (ix) Whether correct entries are passed on issued/ expired/ cancelled Bank Guarantees/ Letter of Credit issued/ expired/ cancelled.
 - (x) Whether there are any bank guarantees continuing even after their period of expiry; if so, ascertain the reasons therefore, and whether

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steps are taken by the branch to close them as per stipulated procedure.

- (xi) Verify the limits/accounts falling due for review, renewal and the action taken by the branch on it.
- (xii) Verify whether Due Date, Diary of review/ renewal is maintained and required follow-up made on those dates.
- (xiii) Verify whether the LCs are closed in the system after full utilization or expiry of the LCs.
- (xiv) While opening LC please verify whether credit report of the beneficiary from approved agency has been obtained.
- (xv) Verify the BG Register/ LC Register carefully and analyse the latest position of BG/ LC.

(G) Foreign Exchange Transactions

- (i) Verify that LC and Bank Guarantee are issued as per terms of sanction and charges are recovered as per FEDAI Rules/ HO Guidelines/ **FEMA Rules**
- (ii) Verify whether branch is adhering to Head Office guidelines issued under delegated discretionary framework of FEDAI.
- (iii) Verify whether all the terms and conditions in the LCs are FEMA compliant, i.e., adhering to the FEMA regulations relating to exports.
- (iv) Verify that packing credit released is backed by LC or confirmed export order. Branch to Ensure that PC (Packing Credit) Stocks are separately shown in Stock Statement submitted.
- (v) Concurrent Auditor to ascertain if D & B Report or Mira Inform Reports are obtained by Branch on the Counter party before disbursing PC or export Bill purchase.
- (vi) Verify whether the drawing power is ascertained before disbursement of Packing Credit (applicable to running account facility).
- (vii) Verify whether the PC is liquidated by either a post shipment finance or from the balances in the EEFC accounts.
- (viii) Verify ECGC cover is available and the ECGC terms are complied with. In case of running packing credit accounts, whether RBI guidelines are complied with.

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- (ix) Concurrent auditor to verify request for remittance on import of Software by the customer. In most of such cases, it is observed that although client has attached CA certificate for software import, no such remittance may be permitted.
- (x) Concurrent auditor to verify those cases where Freight amount to be remitted is more than amount stated in the Shipping Bill. In all such cases if it exceeds 5% tolerance limit, audit may recommend not to remit.
- (xi) In all such cases if it exceeds 5% tolerance limit, he may recommend not to remit.
- (xii) Concurrent Auditor to Report on follow up measures taken by Branch in respect of Export advance received and pending for exports by more than 1 year.
- (xiii) Likewise Concurrent Auditor to report on follow up measures taken by Branch in respect of Imports where Bill of Entry is more than 6 months old, and not available in such cases no second remittance to be allowed.
- (xiv) Verify submission of statutory returns on export/ import transactions, like, BEF (if applicable) statements, XOS (if applicable), write off export bills, R-return, etc. Follow up of outstanding export bills and exchange control copy of bill of entry.
- (xv) Verify whether the branch is following up with the Importers for non-submission of the BOEs, and whether proper records of such follow up are kept at the branch level.
- (xvi) Concurrent Auditor to obtain Export Register to ascertain if any PC or Export Bills are overdue.
- (xvii) Verify whether branches are following up with the exporters for submission of documents where advance remittances towards exports have been received and whether proper records of such follow up are kept at the branch level.
- (xviii) Irregularities in opening of new accounts and operation in NRE, FCNR, EEFC, NRO, etc., and debits/credits entries permissible under the rules.
- (xix) Verify whether operations in FCRA accounts are as permitted by MHA

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and FCRA guidelines.

- (xx) To monitor whether FEDAI rules have been observed in the extension and cancellation of forward contract. Whether competent authority scrutinizes them and the necessary charges, including delivery charges, have been recovered.
- (xxi) Verify whether in case of negotiation/purchase/discounting of Bills under LC, prescribed procedure like, verification of signatures of the Issuing Bank have been followed and scrutiny report issued. Verify booking, utilization, extension and cancellation of forward contracts.
- (xxii) Verify reconciliation of NOSTRO and VOSTRO accounts and verify for random dates that balances in NOSTRO accounts are within the limit prescribed by the bank.
- (xxiii) Verify whether the NOSTRO credits are processed without delay and credit is given to the customer's account on time.
- (xxiv) Verify correctness of charges levied on foreign inward/outward remittances.
- (xxv) Monitor timely/ proper submission of claims to ECGC.
- (xxvi) Adherence to the guidelines issued by RBI/HO about Dealing Room Operations*.
- (xxvii) Verify that the title to goods is in the name of the bank.
- (xxviii) All FCNR receipts are issued by the branch against consideration, i.e., only after receipt of funds. High value deposits need special attention.
- (xxix) Whether rates quoted/applied by the branch on various types of purchase/sale transactions are correct.
- (xxx) Verify that over bought/oversold position maintained in different currencies is reasonable considering foreign exchange operations as well as the extent up to which permission has been given to the branch by the International Division of Head Office for such positions**.
- (xxxi) Payment of ECGC premium/submission of required statements to ECGC for pre-shipment/post-shipment.
- (xxxii) Verification of bill of entry and maintenance of proper records for it.

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- (xxxiii) In respect of overdue packing credits, confirm whether they are Firm Order /LCs. Whether report to ECGC is made and premium is paid, whether RBI's approval is sought in case beyond power of authorized dealer.
- (xxxiv) Whether commercial rate of interest for first day of release is charged for overdue packing credits and those adjusted otherwise than by export bills.
- (xxxv) Verify whether the bills negotiated/discounted/ purchased are within the delegated powers of the branch.
- (xxxvi) Whether export bill negotiated/purchased/discounted is not realized on due date (in case of demand bills within Normal Transit Period and in case of usance bills on the notional due date), exporter's foreign exchange liability should be converted into rupee liability as per policy of individual bank from the notional due date at prevailing TT Selling Rate.
- (xxxvii) In case, additional facility is given to exporter in the form of Packing Credit in Foreign Currency (PCFC) or in the form of Rediscounting of Export Bills Abroad (EBRD) whether conditions applicable to these are complied with.
- (xxxviii) While opening LC please verify whether credit report of the beneficiary from approved agency has been obtained.
- (xxxix) Verify whether there are any instances where the Non-resident Indian maintains a resident account with the bank. (It can be verified by taking a report on Cust-ID level of the customer).
- (xl) Verify whether the branch is adhering to Foreign Contribution Regulation Rules, 2010.
- (xli) Verify whether the guidelines relating to Interest subvention scheme/Interest equalization scheme is adhered to in full.
- (xlii) Verify the reasons for Outstanding Bill and ensure that there is no PMLA activities are involved in those types of Bills.
- (xlili) Verify that the Duty Draw Back has been received by the Exporter on time.

*Applicable only to Category "A" branches.

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** Applicable to both Category “A” & “B” branches.

House Keeping

- (i) Verify Exceptional Transaction Reports are generated and verified by the branch staff as prescribed. Critically analyse the contents of the report also.
- (ii) Review of all balance sheet heads and outstanding entries in accounts, e.g., suspense, sundry and inter-bank accounts. Review of follow up of entries pending for reversal.
- (iii) Scrutiny of daily vouchers with more emphasis on high value transactions and debit entries in suspense account.
- (iv) Verify debits in accounts where signatures are pending for scanning.
- (v) Verify whether records related to KYC/vouchers and other critical areas are sent to specific places like, archival centre, record room as per stipulated periodicity.
- (vi) Verify adherence to KYC/AML guidelines in opening fresh account and subsequent modifications of records and monitoring of transaction.
- (vii) Listing out the Book/Register/Ledger/General Ledger Account heads not checked and/or not balanced. Latest balances taken, amount of balances short/excess, balances differences freeze out, if any, with remarks and actions taken.
- (viii) Whether the branch regularly follows up the outstanding entries for early elimination. Whether any non-prescribed transactions/ extraneous entries in violation of guidelines have been routed through the Sundry Debtors account.
- (ix) Suspense accounts (Sundry debtors) at the branch do not contain any extraneous entries pertaining to clearing cheques returned as it may be an attempt to conceal TOD. Special attention need be given at the end of June, September, December, March for entries of inward clearing cheques parked for the purpose of inflating deposit figures.
Note: Test check a few entries for ` 10,000/- and above as to whether they relate to authorized transactions and authenticated by the branch head. Verify entries in suspense accounts for entire period.
- (x) Ensure that all the Circulars have been properly filed in a separate file.

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- (xi) Ensure that the Details of Duplicate Keys are easily available for verification.

Merchant Banking Business

- (i) Verify, where the branch acts as a collecting branch for issue business, the instructions given by the controlling branch are properly followed.
- (ii) Verify whether daily collection position is advised to the controlling branch.
- (iii) Verify the funds are transferred to short deposit account as instructed and particulars of individual short deposits are advised to the controlling branch regularly.
- (iv) Verify final certificates are submitted properly and in time to the controlling branch.
- (v) Verify that the entire funds collected are remitted to the controlling branch, inclusive of amounts matured, the short deposits and interest thereon giving complete details of break-up of aggregate amount.
- (vi) Verify that the branch does not accept applications from investors after the stipulated closing date of the issue.
- (vii) Verify where the branch acts as a controlling branch, the terms and conditions on which the branch has accepted the role of banker to the issue are complied with.
- (viii) Verify that there is no delay in the issue of final certificates by the branch in its capacity as controlling branch.
- (ix) Verify whether the prescribed preventive vigilance measures are duly observed by the branch.
- (x) Verify where data entry or data processing work is entrusted to outside agencies, the competent authority duly approves these, and the prescribed stamped indemnity has been obtained from such agencies.
- (xi) Verify that it is ensured that dividend interest warrants/refund payment accounts of companies are funded prior to dispatch of the relative warrants by the companies and there is no misuse of the facility. Verify whether deviations, if any, have been made after obtaining the approval of the competent authority.
- (xii) Verify that branch is correctly recovering of the commission/ fees and

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out- of-packet expenses from the concerned companies. Verify whether the competent authority has duly authorized any waiver or reduction of such charges.

- (xiii) Verify claims for reimbursement of amounts of paid warrants received from paying branches are processed and debited to the concerned company's account promptly. Cases of inordinate delays in raising debits, if any, are mentioned.
- (xiv) Verify whether charge on security has been created, wherever debenture trustee activity is undertaken by bank.

(K) Credit Card/ Debit Card

- (i) Verify that the application for the issue of credit card has been properly examined and record of issue of the same has been maintained.
- (ii) Ensure that the charge-slip is examined to verify that it does not cover any picked-up card.
- (iii) Ensure that the overdraft/ debits arising out of the use of credit cards are promptly recovered and higher authorities are invariably informed about the same.
- (iv) Verify that the bank maintains a proper record of picked-up cards.
- (v) Verify that undelivered credit cards are properly kept as security items and followed up with credit card department for further instructions.
- (vi) Carry physical verification of ATM cards, debit cards, credit cards, passwords and PINS, control over issue and delivery, safe keeping and custody at all the locations. Report loss of any such items.
- (vii) Auditor shall verify the custodian of cards and pin mailers are separate.

(L) Accounts with Other Bank

- (i) Verify whether large idle balances are maintained with banks and if so, the amount and for what period at a stretch. Ensuring that the branch obtains full particulars of debits/credits in the account and entries are promptly recorded.
- (ii) Verify and review balance confirmation and reconciliation for accounts in other banks, periodically as specified by the bank.
- (iii) Verify the HO permission to open the account with other banks and

read the terms and conditions.

(M) Documentation

- (i) Whether documents register, or any other similar record, if prescribed by the bank is maintained up to date. Entries are made in this register and found in order. If there is any omission, it should be reported.
- (ii) Verify that all documents have been correctly executed in the latest revised prints of prescribed formats and properly stamped, wherever necessary, in terms of Stamp Act of the respective state, as per manual on documentation and as per circulars on the subject.
- (iii) Where immovable properties are held as security by way of deposit of title deeds, verify title deeds register to see whether narration is written for additional limits and all formalities have been complied with and verify:
 - that original title deeds are with the bank.
 - legal vetting by the bank's empanelled advocate has been carried out with an unconditional confirmation by the advocate that a valid equitable mortgage can be created.
 - certified copy of chain of property with confirmation of the advocate having verified documents available in the municipal records for the number of years as prescribed by the banks.
- (iv) Whether legal opinion and valuation by the bank's advocate/ valuer are obtained for all the mortgaged properties, and the latest Encumbrance Certificate as well as tax receipts is obtained up-to-date and valuation has been carried by the specified value as prescribed by the bank.
- (v) Proper recording of extension of the charge of equitable mortgage for enhanced credit facilities and/ or other credit facilities has been complied with.
- (vi) Verification with CERSAI records should be carried out before disbursement/creation of mortgage as applicable.
- (vii) Verify whether signature of executants/property owners are available on letter of confirmation of creation for having created equitable mortgage on the record.
- (viii) In the case of company/ limited liability partnership (to the extent

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applicable):

- Whether copy of resolution passed by the company's board is on record for availing the credit facilities from the bank.
- Whether the authorized signatories as mentioned in the board resolution have executed the documents.
- Whether common seal, if applicable, has been affixed on the relevant document.
- Whether bank's charge or modification thereof has been registered with the Registrar of Companies (by filing Form 8).
- Whether search report of company's earlier charge has been made.

- (ix) Check classification of advances as per RBI's Prudential Norms.
- (x) Wherever registered mortgage has been prescribed in terms of sanction, verify whether the same has been carried out properly.
- (xi) Auditor must see whether "Vetting of Documents" has been carried out as per HO directives.
- (xii) Auditor must ensure that no documents are "Time Barred" and satisfy that all the documents are "Enforceable Before Court of Law".

(N) Renewal of Documents and Time Barred Accounts

- (i) Verify limits/accounts falling due for review, renewal and action by the branch.
- (ii) Verify whether due date diary of review/renewal has been maintained and required follow up has been done on those dates.
- (iii) Whether the debts/decrees are time barred. Action taken to be commented upon.

(O) Bills Purchased/ Discounted/ LCBR (Import LC Documents)

- (i) Verify whether bills purchased/ discounted are genuine trade bills accompanied by lorry receipts of IBA approved transport operators; or railway receipts or airway bills or bills of lading or any other approved mode of transportation, and prima facie no unhealthy features are observed in the transaction.

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- (ii) Verify whether any bills purchased/ discounted/ negotiated were returned unpaid and if so, whether they are properly dealt with, and reimbursement has been obtained promptly including interest at applicable rate. If the reimbursement is not prompt, verify whether the same has been reported.
- (iii) (In case there are frequent returning of bills for huge amounts pertaining to a borrower, verify the reasons thereof and whether such cases have been reported to the concerned sanctioning authority).
- (iv) Verify the bank guidelines for bills once discounted and returned are not again discounted.
- (v) Verify that there is proper follow-up of overdue bills.
- (vi) Verify the realization advice adjusted in respect of outward bills realized (purchased/ discounted/ negotiated/collected for large amounts (say 10.00 lakh and above) as to genuineness of the adjustments.
- (vii) Whether in the case of bills purchased/ discounted/ negotiated the liability is within the limits. Verify that such transactions with allied/sister concerns are allowed if specifically permitted.
- (viii) Whether any excess drawings/ bills beyond the sanctioned limits/ drawing power are allowed and if so, whether the branch has forwarded ratification/ confirmation of the concerned sanctioning authority. Whether such excesses are under the authorization of the branch head and properly recorded in the prescribed register and reported to the appropriate authorities.
- (ix) Verify whether there are any bills purchased/ discounted/ negotiated outstanding beyond a reasonable period/ beyond due date and observation of any unusual/ unhealthy feature; ascertain reasons for overdue and whether reported to the concerned authorities in the prescribed manner.
- (x) In respect of bills purchased/discounted/negotiated, whether goods are appropriately protected with insurance.
- (xi) Whether credit report on drawers in respect of bills and drawers in respect of cheques is obtained?
- (xii) Whether LC documents were verified with LC terms? Whether LC bill was rejected by the importer for any reason of non-compliance with LC

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terms, etc.

- (xiii) Whether cheque/bills are dispatched promptly, at least on the next day.
- (xiv) Whether interest/commission, as prescribed, has been collected?
- (xv) Does the branch ensure dispatch of returned cheques by registered post if they are not collected immediately? In case any deviation is noticed, please give full details.
- (xvi) For supply bills, verify whether the branch ascertained the genuineness of the underlying contract and power of attorney registered in the bank's favour.
- (xvii) What is the system of follow up for the recovery of returned bills? How long have they been kept pending?
- (xviii) Are the goods covered generally traded items/dealt with by the borrower?
- (xix) Verify in respect of all overdue and returned bills (including bills under LC), action taken by the branch is as per the guidelines.
- (xx) In respect of export bills purchased/discounted, expressed in foreign currency, whether overdue bills were promptly converted into rupees under report to the central office.
- (xxi) Whether packing credit was adjusted out of export bills purchased.
- (xxii) Comment on cases where payment has been received under reserve.
- (xxiii) ECGC policy as applicable is held, and buyer wise limit is complied with.
- (xxiv) Whether appropriate margin has been maintained as per sanction terms.
- (xxv) Whether the turnover in bills limit reflects the true position of sales as evidenced from financial statements. Large variation should be commented.
- (xxvi) In case of foreign bills purchased/ discounted for export on FOB and C&F terms, whether the contingency risks policy is as per Head Office instructions.

(P) Cash Credit Including Temporary Overdrafts

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- (i) Verify whether the branch has identified and classified the advance in accordance with the guidelines of the RBI and the Head Office.
- (ii) Report individually on accounts in which there are irregularities due to:
 - (a) Excess drawing over drawing power.
 - (b) Excess drawing over limit.
 - (c) Deficiency in documentation.
 - (d) Operations unsatisfactory/no operation.
 - (e) Drawings against unclear effects.
 - (f) Non-recovery/absorption of interest.
 - (g) Not covered by sanction.
 - (h) Unreported excesses.
 - (i) Drawings not reflected by QIS where applicable.
 - (j) Account not brought to credit as per sanction terms.
- (iii) Verify whether passing of cheque is duly authorized through Cheques Referred Register, and whether there are irregularities as mentioned above.
- (iv) Whether excess over the limit/drawing power is covered by adequate security and prescribed margin is maintained.
- (v) Whether sundry creditors are reported in stock statement are deducted to calculate drawing power against paid stocks.
- (vi) Whether any spurt in inventory is noticed and verified for the source of funds.
- (vii) Whether norms for inventory and receivable, wherever applicable is being monitored.
- (viii) Whether appropriate action has been taken where the non-submission of stock statement persists for more than two months.
- (ix) QMR/HMR are studied critically, and date are entered in a register for follow-up at the time of annual review. Whether variations from projections are analysed and considered realistic, based on past performance and environmental outlook. A concurrent auditor needs to

Concurrent Audit Checklist

verify the adequacy/enforceability of insurance or insurable assets with appropriate risks, location, etc. The concurrent auditor needs to indicate cases where a delay in the recovery of interest has been noticed. Ad hoc facilities allowed to continue beyond the stipulated period mentioned in sanction, also need to be highlighted. Excess beyond the ad hoc limit without report/confirmation and allowed to continue without recovery to be pointed out.

- (x) In case, specifically mentioned by the bank, the concurrent auditor should conduct inspection of units/ godown/fixed assets/stocks under pledge and hypothecation in such a way that all the accounts are inspected as terms of appointment letter at least once in every six months. Stock inspection report should be in the prescribed format of the bank for this purpose.
- (xi) Ensure that CC Limits have been renewed on time with necessary papers.
- (xii) Ensure that CC Limits must be renewed within a period of 180 days from the original due date of the loan, otherwise that CC Limit will become NPA as per IRAC Norms.
- (xiii) As per RBI Circular, the sanction letter should clearly mention the “Due Date” of the Loan. The auditor must ensure that due dates have been properly mentioned in the sanction letter.

(Q) Advances under Consortium Arrangement

- (i) Verify whether consortium meetings are held and minutes of meeting are prepared. Verify whether minutes of the meeting are communicated to all consortium members. The branch keeps the controlling office informed of all the meetings and deliberations.
- (ii) A confirmation from the lead bank that original documents are held by the bank on behalf of all the member banks. Securities are created by them on behalf of all member banks and equitable mortgages are held by them on behalf of all banks.
- (iii) Joint inspections of the unit/stock are carried out as per joint lender's agreement. Verify that the irregularities in the inspection report are promptly attended to.
- (iv) Verify that pro-rata business, including non-fund-based business, is

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transacted through the bank.

(R) Refinance Management (NABARD/ SIDBI/ Exim Bank)

- (i) Whether all eligible term loans disbursed has been identified and reported to competent authority without delay.
- (ii) Whether the commercial rate of interest has been charged till the date of refinance.
- (iii) Whether the branch has ensured that the claim is in order.
- (iv) Whether the branch has been kept informed by the principal account holder and those liable under the counter guarantee.
- (v) In respect of Deferred Payment Guarantee, whether payment is made to the debit of party's account on due date without creating overdraft/debiting suspense.

(S) Verify Balance with Other Banks

- (i) The auditor must verify all large idle balances with other banks. The period and amount with other banks must be verified with the records. Auditor must ensure that all the details of the transactions are obtained from other Banks.
- (ii) The auditor must verify that Other Bank statement and compare the same with the Bank and in case of any difference, the auditor must get it reconciled with the help of the branch Manager.
- (iii) Verify balance confirmation with another Bank.
- (iv) Verify the letter of authorization issued by HO/ZO/RO to open the account with another bank by the branch.

(T) Other Assets/ Sundry Creditors/ Accounts

- (i) All Pension Payment Order (PPO's) are properly numbered and recorded.
- (ii) Records at branch for pension payment order are up to date. Verify whether any excess pension payment is outstanding in branch for recovery.
- (iii) Verify whether link branch (if applicable) is sending pension payment scroll to RBI/SBI well in time for reimbursement.

Concurrent Audit Checklist

- (iv) Verify whether, every November, Life Certificate has been obtained in case of all PPOs.
- (v) In case of undisbursed pension, check that the amount has been promptly returned.
- (vi) Whether TDS has been deducted as per extant rules.
- (vii) Whether turnover commission is recovered by the link branch and distributed amongst branches.
- (viii) Whether reimbursement is in arrears.
- (ix) For collection of taxes, PPF A/c, etc. whether funds received are immediately remitted to link branch.
- (x) Ensure at least 30% scrutiny of transactions relating to the payment of pension has been done.
- (xi) Whether the prescribed certificates - Life, Re-employment, Re-marriage, etc. has been obtained, wherever required, in all pension accounts.

(U) Others – Verify

- (i) Compliance of provisions relating to tax deducted at source, service tax, trade tax, other duties and tax.
- (ii) Physical verification of inventory, control over issue of inventory, safe keeping and custody of security forms. Report any loss of such items.
- (iii) Physical verification of other deliverable items, control over issue, safe keeping and custody.
- (iv) Physical verification of gold coins, control over issue, safe keeping and custody. Checking of gold sale transactions.
- (v) Custody and movement of branch keys.
- (vi) Locker keys and locker operations – linking of FDR as security for locker/ operation of locker/ inoperative lockers/ nomination/ other issue.
- (vii) Safe custody of branch documents like, death claim cases, issuance of duplicate DD/PO/FDR, checking of indemnities, etc., and verification of documents executed during the period under audit.
- (viii) Reporting of frauds.

General Banking- Income Tax/ Service Tax/ GST/ Other Tax Related Issues

- (i) Verify the transactions where 'PAN' is mandatorily to be submitted under Rule 114 B of the Income Tax Rules, 1962. In case where such person does not have 'PAN' he shall make a declaration in Form 60, giving therein the particulars of such transactions. The transactions are:
 - (a) A time deposit with banking company for an amount exceeding ` 50,000/- or aggregating to more than ` 5 lakh during a financial year.
 - (b) Opening an account other than as mentioned in (i) above and a Basic Saving Bank Account.
 - (c) Making an application to any banking company for issue of credits or debits cards.
 - (d) Deposit with a banking company of cash exceeding Rs. 50,000/- during any one day.
 - (e) Purchase of bank drafts or pay orders or banker's cheques from a banking company where payment was made in cash for an amount exceeding Rs. 50,000/- during any day.
 - (f) Payment against purchase of any foreign currency at any time, in cash, of an amount exceeding Rs. 50,000/-
 - (g) Payment against sale/purchase of goods/ services for amount exceeding Rs. 2 lakh per transaction.
- (ii) Verify whether banks which have received any declaration in Form No. 60, as stated in para 'a' above, on or after 01-01-2016 in relation to any of above transactions referred to in Rule 114 B of Income Tax Rules, 1962 shall:
 - (a) retain such Form 60 for a period of 6 years from end of financial year in which transaction was undertaken, and
 - (b) furnish a statement in Form No. 61 to the Director of Income tax (Intelligence and Criminal Investigation) or the Joint Director of Income Tax (Intelligence and Criminal Investigation) through online submission of electronic data to a server designated for this purpose and obtain an acknowledgement number thereof.

Concurrent Audit Checklist

- (c) Such filing of Form No. 61 is to be made within prescribed time, i.e., up to 31st October for declarations received up to 30th September and up to 30th April for declarations received from 1st October to 31st March.
- (iii) Verifying the obtention of PAN and updating of the same in computer.
- (iv) Verify whether fixed deposit of Rs. 20,000/- or more has not been repaid in cash. This is in contravention of provisions of Section 269T of Income Tax Act, 1961. In case repayment is made by any branch of a banking company, such repayment may also be made by crediting the amount of such loan or deposits to the saving bank account or current account with such branch.
- (v) Verify whether the compliance of section 206AA of Income Tax Act, 1961 has been made with regards to furnishing of 'PAN'.
- (vi) Verify the compliance of issues relating to TDS on salary, pension, disbursement, rent, commission, interest, payment to contractors, payment of fees to professional/technical person, etc. in respect of:
 - Deduction of TDS at correct rate.
 - Deposit of TDS within time.
 - Filing the TDS return in time and as per procedure prescribed.
 - Issue of TDS certificates.
 - Receipt of 15G and 15H and entry in system.
 - Filing of Form 15G/ 15H with department as per new procedure.
- (vii) Ensure whether Form 15CA and 15CB has been obtained for outward foreign remittance and filing of details of these forms in Form 15CC as per Rules 37BB which states that banks shall furnish a quarterly statement for each quarter of the financial year in Form No. 15CC as per procedure given in Rule 37BB.
- (viii) Ensure that no payment has been made exceeding Rs. 20,000/- against an expenditure otherwise than through an Account Payee Cheque or Account Payee Bank Draft to comply with provisions of Section 40 A (3) of the Income Tax Act, 1961.
- (ix) Ensure compliance of service tax, trade tax and other duties and taxes.

ESG Reporting (Environmental, Social, and Governance)

Banks and financial institutions are now expected to report their sustainability practices, including how they manage:

- Environmental (energy, waste, emissions).
- Social (customer responsibility, diversity, community).
- Governance (ethics, compliance, board structures).

Also refer to the circular RBI ESG & Climate Risk Circulars (2023).

Although ESG reporting is typically at Head Office level, branch-level inputs are critical.

Concurrent Audit Focus Areas:

- (i) Data Accuracy and Source Validation.
 - Verify correctness of data provided by the branch on.
 - Power consumption.
 - Paperless banking initiatives.
 - CSR or financial literacy camps.
 - Ensure it is supported with documentary evidence.
- (ii) Compliance with Environmental, Social and Governance (ESG)- related policies:
 - Check whether bank's Green Banking policies or social outreach guidelines are being implemented.
 - Check whether the branch has followed ESG- linked loan conditions/ prohibited industries as specified in RBI circular (e.g., no lending to polluting industries, no lending to industries using/ producing ozone depleting items).
- (iii) Governance Indicators:
 - Examine internal controls, staff training records, and grievance redressal metrics.
 - Ensure any ESG-related complaints or incidents are recorded and reported.

(iv) Lending and Risk Practices:

- Are borrowers being evaluated on ESG criteria?
- Check whether the branch has classified ESG non-compliant borrowers as higher risk, if applicable.

Digital Lending

Digital Lending involves end-to-end processing of loans through digital platforms — often including third-party apps, APIs, and automated underwriting.

Concurrent Auditor should refer to the master directions on digital lending issued by RBI. Ref no. 2025-26/36 dated 08/05/2025 and ensure the compliance of the same.

Fintech Partnerships

Banks collaborate with fintech's for products like:

- Loan origination platforms.
- Buy Now Pay Later (BNPL).
- Co-lending arrangements.
- Payment solutions and customer engagement tools.

Concurrent Audit Focus Areas:

(i) Outsourcing Risk Management:

- Check whether the bank has entered a formal agreement/MOU with the fintech.
- Verify whether the bank's outsourcing policy is followed (per RBI guidelines).

(ii) Data Privacy & Security:

- Ensure customer data shared with fintech's is:
- Within the scope of the agreement.
- Protected by adequate cybersecurity controls.
- Not misused for cross-selling.

(iii) Revenue Recognition:

- Cross-check income received from fintech collaboration — referral fees, servicing income, etc.
- Whether charges are levied by the fintech (if any) being properly disclosed to the customer.

(iv) Co-Lending Compliance:

In case of co-lending, verify:

- Risk sharing ratio.
- Joint loan agreements.
- Reporting to CICs (Credit Information Companies).
- Proper accounting of bank's share in the CBS.

(v) Customer Experience and Grievances:

- Ensure that a mechanism exists for redressal of customer complaints in fintech-led journeys.

Checklist - Quarterly

Revenue Checking

Verify and report non-recovery of:

- (i) Locker rent.
- (ii) Folio charges.
- (iii) Penal charges for delayed/ non-submission of returns, financial statement/ stock statement required to be submitted.
- (iv) Penal charges on advances in respect of lapsed sanction/ limit.
- (v) Penal charges on excess over limit.
- (vi) Overdue interest on all types of bills, loans and packing credits for overdue period.
- (vii) Commitment fee for unutilized limit is collected as per rules.
- (viii) Commission of letter of credit, letter of guarantee and charges for safe

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custody, etc.

- (x) Standing information charges.
- (xi) Stop payment charges.
- (xii) Processing fee on advances.
- (xiii) CIBIL charges, if applicable.
- (xiv) Lead bank charges.
- (xv) Cheque returns charges.
- (xvi) Inspection charges.
- (xvii) Charges for documents under LC.
- (xviii) Charges for any services provided.
- (xix) Cheque-book issue charges.

For rates, the bank's service charges booklet/manual should be obtained and kept on record during the period of audit.

Checklist- Half yearly

Following is an illustrative half-yearly checklist:

- (i) Physical verification of government and other securities held on behalf of Investment Department and timely collection of interest thereon and their maturity proceeds.
- (ii) Compliance with insurance limit for cash and other fixed assets of branches.
- (iii) Fixed and other assets at branch are serially numbered and recorded in fixed assets register, are adequately insured. Depreciation is calculated at head office or branch wise.
- (iv) If office building is rented then check that rent agreement has been kept in safe custody, and the same has been renewed timely.
- (v) Check whether customer service is satisfactory regarding the following areas:
 - Customer meeting has been convened as prescribed.

- Standing instructions are followed up.
- Complaint/suggestion box has been kept in branches.
- Staff dealing with customers at branch is polite to customers.

Checklist – Yearly

- Physical checking of Closing Cash including ATM cash, Adhesive Stamps, Foreign Currency-
- Physical checking of Fixed Assets / Dead Stock items-
 - (a) Joint verification with Manager at the year end and to put remarks on the respective register/statement.
 - (b) Whether Depreciation is calculated and accounted properly?
- Branch Shop Act License (If applicable) -
- Whether Renewed? If Yes, Renewed up to which period?
- Duplicate set of safe keys - Last exchanged on.
- To confirm whether AMC register is available at branch and updated regularly.

Provisioning entries - rent, electricity, telephone, water bill, etc

Unclaimed Valuables:

1. Whether proper register is maintained and updated for unclaimed valuables found in bank premises.
2. Verify any undertaking or declaration or any precautionary measures taken as per policy.

Chapter 2

Core Banking System

Background

- (a) Over the years, the banking operations have been largely atomized, and wide range of banking software's have been developed for accounting of transactions and core banking operations.
- (b) Bank software's are becoming more sophisticated all the time.
- (c) As new accounting methods develop and more people bank online, private banking software is being developed to streamline the processes.
- (d) This is a Revolution in Banking Industry, as the Manual System of Maintaining accounts was being converted into System Based Maintenance of accounts through the various Software of Banks.

Banking Industry and Banking Software

Current Scenario

- (a) The face of banking industry is changing continuously.
- (b) What Banking is today is quite different from what it was in the years gone by.
- (c) Some of the present trends in banking industry include following:
 - (i) Focus on Customer Relationship (Service Oriented Architecture [SOA]).
 - (ii) Introduction of Value-Added Services.
 - (iii) Connectivity of branches.
 - (iv) Multiplicity of Delivery Channels (ATM, Cash Deposit Machines, Cheque Deposit Machine, Point of Sale Units, Credit Card, Mobile Banking, Internet Banking).
 - (v) Focus on MIS and Risk Management.
 - (vi) Focus on Reduction of Transaction Cost.

Future Scenario

- (a) One can visualize future scenario in the industry on current trends.
- (b) Going by the current happenings one can expect the future of banking industry.
- (c) Some of the important factors are as follows:
 - Increase in the expectations of customers.
 - Increase in healthy competition due to issue of new banking license.
 - A greater variety of products and delivery channels in the market.
 - Centralised customer management (Service centric approach).
 - Information technology to act as an integrator and enabler between demands on the industry and services rendered.

Challenges

Challenges – Customers' Expectation:

1. The biggest challenge before the banking industry today is posed by its customers' expectations.
2. The customer today is more informed and aware than before. Customers demand more services and delivery channels.
3. Customer's expectations are increasing with respect to anywhere, anytime banking and for diverse products and facilities.

Challenges – Stiff Competition:

1. There are challenges posed by market forces due to stiff competition wherein the differentiator or selection of bank by the customers is based on quality of services.
2. The service up-gradation comes with a cost for the bank.
3. Hence, a trade-off between cost of transaction and quality service to customer is the key.
4. Moreover, due to diversified products and services, up to date information for customers and bankers is very important.

Other challenges

1. Regulatory Requirements:

On the other front the regulatory requirements are rapidly increasing. Apart from handling transactions, customer and competition it is very important to pay equal attention to adherence to regulatory guidelines.

2. Software Updates and Requirements:

A composite system / software which handles transactions, customer relations, regulatory compliances, MIS/ reports request is the need of the hour. Core Banking Systems (CBS) provide the solution for the same. There are various Core Banking Software's available in the market. More prominent and used in India are Finacle, FLEXCUBE, TCS Bancs.

Audit of Banks and Banking Software

- (i) Ever since the human being started documenting transactions, audit methodology and techniques have evolved over the period keeping pace with the style of business.
- (ii) With the growth in business volume and technological advances there has been paradigm shift in various aspects of business.
- (iii) Conducting audit of financial transactions cannot be an exception to the same.
- (iv) Traditional audit techniques and methodology were outcome of the volume and complexities of the business of its time.
- (v) A classic example of the same is audit techniques applied for conducting audit of a bank operating under Core Banking System (CBS).
- (vi) As we have witnessed, during the last decade there has been large scale growth in banking services, covering more geographical area and large number of populations.
- (vii) This has necessitated applying modern technology, particularly in the field of data capturing, recording and processing. CBS is outcome of the same.
- (viii) For obvious reasons audit methodology cannot remain static, it has also to change. Therefore, with the spread of CBS in large number of cases, changing audit methodology also became inevitable.

- (ix) If the auditor's dependence on technology hinges heavily, there is no reason why auditor should not apply the same technology.

Core Banking Solution (CBS)

- (a) The core banking system is the set of basic software components that manage the services provided by a bank to its customers through its branches (branch network).
- (b) The bank's customers can make their transactions from any branch, ATM (of the Same Bank or other Bank), service outlets, internet, phone at their disposal.
- (c) The CBS is based on Service Oriented Architecture (SOA).
- (d) It helps banks to reduce risk that can result from manual data entry and out of date information.
- (e) By restricting any Data to be entered one single time in the system, Data Integrity must be ensured.
- (f) When any modification of Data is entered, and the details of Entry/Modification/Deletion/Approval are required, and the transactions are not completed unless and until the same is approved/rejected at the Higher Level.
- (g) The Approved Data is incorporated in the Database.
- (h) It also helps banks to improve service delivery quality and time to its customer.
- (i) The software is accessed from different branches of bank via communication lines like, telephones, satellite, internet, etc.
- (j) Core Banking System (CBS) works on a concept of Centralized Database and Processing.
- (k) Transactions take place at various geographical locations which get recorded and processed at a Centralized Server.
- (l) Updating of database is on Real Time Basis.
- (m) Due to the centralization of transaction processing, issue of out-of-date information is eliminated. All the users connected to CBS will be able to get up to date information.
- (n) CBS also enhances quality of reporting and strengthens access control.

Centralized Banking Solution/ Core Banking Solution

- (a) Under CBS, data is stored in centralized servers at data centre. This effectively means that all operations at the connected branches, back offices are carried out through servers at data centre including transactions through other delivery channels like, ATMs, internet banking, phone banking, UPI through Mobile etc.
- (b) Under CBS, the branches, back offices are defined as SOL (i.e., Service Outlets) where each SOL functions as a service window.
- (c) The CBS can process any transaction from any branch location connected to CBS.
- (d) It can be equated with single window operations at airline counters or railway reservation counters wherein all the services can be obtained at one place.
- (e) Hence, under CBS customer is now a customer of the bank and not merely a customer of a branch of the bank.
- (f) This has facilitated anywhere, anytime banking convenience for the customer.
- (g) CBS made one branch customer as the “Entire Bank’s customer and this is the starting point of “anywhere and anytime Banking convenience” for the Bank customer. This creates the feeling of lot of comfort and safety to the Bank customer.
- (h) From the bank’s perspective, control over the application and processes has been entrusted at data center level.
- (i) In addition to it, CBS also makes available effective MIS on a real-time basis.
- (j) It enables generation of all periodical returns centrally.
- (k) As mentioned above, there are various CBS developed by various software companies available in the market and most used are FINACLE, TCS Bancs and Flex Cube.

Introduction to FINACLE

- (a) A Financial Package, for banking solution developed by Infosys on a platform of Oracle, is thus named as FINACLE.

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- (b) Presently, many Indian Public Sector Banks, Private Sector Banks and Foreign Banks operating in India are using this software as banking solution due to high flexibility and scalability.
- (c) Finacle is an integrated, on-line, enterprise banking system designed to provide the "e-platform".
- (d) Prior to 1995 it was known as BANC 2000, a Total Branch Automation package with a distributed network. After 1995 Infosys developed the same as FINACLE, a Core Banking Solution.
- (e) Functionalities of Finacle are as follows:
 - Finacle facilitates anywhere banking.
 - It is menu driven software with easy navigation.
 - It is functionality rich and addresses the retail and corporate banking requirements.
 - Customization and parameterization are two special features of Finacle.
 - Finacle provides multi-lingual support.
 - Finacle provides multi-level security, i.e., operation, database and application-level security.
 - It supports workflow-based transaction processing.
 - It has high level of security control and audit capabilities.
 - It has a common transaction interface for all type of transactions.
 - It provides a browser-based GUI interface to Finacle.
 - SQL and PL SQL is used for generation of MIS, reports, queries at centralized level.
 - Designed for optimum usage of network bandwidth.
 - There are two functional modules:
 - *Retail and Corporate Module*- Encompassing Saving Accounts, Current Accounts, Term Deposits, Cash Credit Accounts, Overdraft Accounts, Term Loans, Demand Loans.

- *Trade Finance Module* - Encompassing Inland & Foreign Bills, Forward Contracts, Inland & Foreign Documentary Credits, Inland & Foreign Bank Guarantees, Inland & Foreign Remittances and Pre-shipment Credits.

Security in Finacle

FINACLE is having multiple levels of security. Various security levels embedded in it are as follows:

1. OS Level:
 - No access to OS
 - OS and application-level profile
 - Direct login to application menu
2. Database level:
 - Protection from external updating
3. Application level:
 - Menu level
 - User level
 - Product level
 - Account level
 - Transaction level
4. Dual control for all transactions:
 - Maker-Checker Concept
5. Controlled error handling through exceptions:
 - (1) Warning (2) Exception (3) Error

Finacle Overview

Following is an overview of Finacle for understanding of the users:

Finacle User Menu								
Menu Block			Favorites					
Main Menu -> Sub Menu -> Menu Description [Menu Code]			User Defined Favorites					
MESSAGE AREA								(A)
Menu Option	(B)	Btn.1	Btn.2	Btn.3	Btn.4	Btn.5	Btn.6	Btn.7
Action Bar								

A = Progress Indicator

B = Field to Specify Menu Option

- *Menu Block*: The block houses all the menu and sub-menu options available in Finacle.
- *Menu Option Block*: Menu Code to be entered to gain access to the respective menu.
- *Action Bar*: User can execute the process of Finacle operations by clicking on various options on this bar. The hot keys are also assigned for all options, which appear on the bar.
- *Action Buttons*: Every action button has a specific purpose. For e.g., on clicking Who Ami button, system will display use rid of the user who is currently logged in and other information, viz., date and name of SOL in a message box.
- *Message Bar*: The message bar displays warnings, exceptions, errors or lists under a specific field code.
- *Favourites*: Menu items which are required and used on regular basis can be put in favourites by copying from Menu Block. As onetime process, specific menu item which is required to be copied to Favourites should be in menu block and with the use of drag and drop the function can be stored under favourites menu.

- *Progress Indicator:* It shows the progress of the action initiated using colours (i.e., **Green** indicates that the System is “Ready” for processing, **Red** indicates that the “System is busy in Processing Activity” and **Yellow** indicates that browser is performing internal processing like, assembling/ painting screen as per requirement. User should not operate the system).

General Key Map

Default Physical Keys in Finacle have been given in the table below. However, default key map differs in individual bank.

Physical Key	What does it do?
F1	Field level help. Like in several word processors and spreadsheet packages, F1 displays context sensitive help messages and field level help messages.
F2	List. This key lists the codes that may be used in a particular field.
F3 / ESC	Quit/ Back. Quits and takes the user back to where he started when in action. It can be used when the input is incorrect, and the user wants to abandon what he has been doing. It can also be used to go back to the previous menu.
F4	Accept. After the user has completed the input, this key can be used to accept the data.
F5	Background Menu
F6	Next Block
F8	Copy Record
F9	Display Signature
F10	Commit/ Save. This is a very <i>important</i> key, and this concludes the transactions. This is the commit, and transactions get into the General Ledger (database) when this key is used.
F11	Next field

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F12	Previous Block
TAB	Go to the next valid field
ENTER	Go to the next field
DOWN Arrow ↓ (Next Rec button)	Next Record (In a list or result of a query)
Up Arrow ↑ (Prec Rec button)	Previous Record (In a list or result of a query)
CTRL+F1	Help maintenance
CTRL+F3	Show key map
CTRL+F4	Display error
CTRL+F8	Terminal lock
CTRL+F9	Memo pads look up
CTRL+F11	Context level help
CTRL+D	Page down on a list
CTRL+E	Explode. This key is particularly useful for further inquiry.
CTRL+F	Clear field. This key combination can be used when the user wants to clear the field.
CTRL+T	Display LGI. The user ID, Terminal ID, SOL, BOD Date and language details are displayed.
CTRL+U	Page up on a list
CTRL+X	Put a BOD date. This key combination populates the default BOD date in the field.
SHIFT+F4	Select the current item from the list. This key combination can be used to select a value from the list of valid values listed for a particular field.
SHIFT+F11	Transmit
SHIFT+TAB	Go to the previous field

Introduction to TCS Bancs

- (a) A Financial Package, for Banking Solution offered by Tata Consulting Services. The Core Banking solution TCS Bancs is an integrated solution that automates all aspects of core banking operations across entities, languages and currencies.
- (b) Bancs are built on open architecture, component-based product suite to leverage service-oriented and event-driven architectures.
- (c) Its functionalities are as follows:
 - Entire range of banking products including savings, checking, overdraft and deposit accounts.
 - Entire range of lending products.
 - Complement of transactional services including remittance, foreign exchange, cards and trade finance.
 - Accessibility through multiple channels, including mobile banking and web.
 - Full integration of front, middle, and back-office processes.
 - Accurate, timely and actionable information about customer relations.
 - Single view between bank and customer.
 - “Anytime anywhere” banking.

Introduction to Oracle Flex Cube

Flex Cube provides a comprehensive, integrated, interoperable, and modular solution that enables banks to manage evolving customer expectations. Major functionalities are as follows:

- 24/7 processing of large transaction volumes, with high availability.
- Multiple delivery channel support.
- Security management covering application and role-based access.
- Service-oriented architecture supports agile business process management.
- Componentized architecture helps build scalable and reusable solutions.

Quick Access Screens through Hot Keys in Flex Cube

Hot Keys	Screen Name	Description
Alt + B	Balance Inquiry	This screen displays the account details of the savings and checking account balances such as the available balance, nucleated balance, current. Book balance, passbook balance, net balance, etc.
Alt + C	Customer Name and Address Inquiry	This screen displays details such as the name, address, city, country, SSN/TIN number, etc., of the selected customer.
Alt + A	Account Details	This screen displays the account details of the customer such as account number, account branch, account currency, customer name, etc.
Alt + S	Amount based Account Image Display	This screen displays the images based on the details maintained in the Amount Based Operating Instruction Maintenance (Fast Path: 7116) option.
Alt + P		This will enable the user to print the receipt of the transaction.
F8		This will enable the user to return to the same screen.

General Concepts of CBS and Finacle

SOL ID and Set ID (Init. Br. ID)

- a. **SOL ID** -Under Core Banking System, each Branch, Back Office, Administrative/ Controlling Office are assigned a code, i.e., Service Outlet ID [SOL ID]. It helps in identifying the Branch / Office under which the Account is maintained. Hence, if a branch at Delhi is assigned a SOL ID of “0089”, the accounts opened under Delhi Branch will display “0089” as SOL ID in CBS.

- b. As discussed above under CBS any branch can initiate transaction for any of the account maintained with the bank. Hence, a distinction is required between the branch which maintains the account and the branch who initiate the transaction.
- c. **Set ID (Init. Br. ID):** Set ID or Initiating Branch ID is a SOL ID of the Branch who initiated the transaction. For e.g., transaction of a cash withdrawal by a customer of Mumbai Branch (SOL ID “0044”) from Delhi Branch (SOL ID “0089”). In the instant case “0089” is Init. Br. ID and “0044” is Account SOL ID.
- d. To search transactions based on the branch who initiated transactions in Finacle, SET ID (Init. Br. ID) parameter is required to be used under Menu Code “FTI”.

Tran ID, Journal No. and Date

- a. Each transaction in Finacle will be assigned a unique Transaction ID.
- b. The Transaction ID remains unique only for the day, since, on the next day the Transaction IDs are reset.
- c. Combination of Transaction ID and transaction date make it unique across the system.
- d. In Finacle, once the transaction is “Entered”, a Tran ID is generated. To locate any transaction from the database the user needs to use Tran ID and Date at TI/TM Menu command.
- e. Under Bance the transaction number is known as Journal Number.

1. Transaction Type and Sub Type

Transactions in Finacle are entered with the Transaction Type and Transaction Sub Type. It is easier to trace a set of transactions with Transaction Type and Sub Type.

Codes for Transaction Type and Sub Types are prescribed differently by each bank. For e.g.,

Transaction Type codes for Cash and Transfer may be of following types.

- Tran Type: Cash: “C”, Transfer: “T”
- Sub Tran Type: CR – Cash Receipt, CP: Cash Payment

The auditor must acquaint himself with the Transaction Types used by each bank. It helps auditors to design query (search parameters) for financial transactions.

Customer Master Level Configurations

1. Under CBS, the customer is identified by a number, generally, called CUST ID/ CIF No. Following are the advantages of separate configuration for customer and accounts of customer:
 - (a) Identification of unique customers.
 - (b) Data redundancy can be reduced by eliminating the process of updating repetitive details about customer at each time of opening of account.
 - (c) It is easier to comply with customer centric regulations. For, e.g., TDS provisions under Income Tax Act (where payment to customer is important than payment for an account), IRAC Guidelines (where classification of account is borrower-wise and not account-wise).
 - (d) Multiple accounts of the customer can be mapped to a customer for better identification.
 2. Under the Customer Master Level configuration basic details about the customer are updated. Details include name, date of birth, PAN number, etc.
 - A. Once the CUST ID/ CIF is opened, various accounts can be opened under the said CUST ID/ CIF. Relationship between CUST ID/CIF No. and account is that of parent and child wherein the Account Master inherits the information and parameter values from Customer Master.
 - B. In Finacle menu command **CUMM/ CUMI** is used for inquiry on CUST ID/ CIF No. Under Bancs the customer master details can be reviewed through "Customer Master Details" module.
- 2.18. Some important points for auditors are as follows:
- (i) Issues with multiple CUST-ID;
 - (a) In terms of guidelines issued by the RBI on UCIC, each customer in the bank is required to be assigned a unique ID.

- (b) However, it has been observed in many banks that multiple CUST IDs have been opened for customers.
- (c) It has also been observed that at the time of migration, it had migrated old customer information to one CUST ID and have opened new CUST IDs for opening of new accounts post migration.
- (d) Due to multiple CUST ID the very purpose of having configuration of CUST ID is defeated.
- (e) The auditors should verify such discrepancies at the time of account opening verification.
- (f) Moreover, the auditors should also seek help from the bank's IT Dept. for a generation of reports based on the combination of information, viz., name, PAN, date of birth, employee code, etc., to identify existing cases of multiple CUST ID in the system.
- (g) At the opening of the account, Finacle automatically displays the name of account holder based on CUST ID details.
- (h) However, Finacle also allows the user to amend the name.
- (i) Generally, the said change is configured as an exception which requires sufficient powers/ work class in the system to override.
- (j) The auditor at the time of Account Opening verification should verify the details as per CUST ID and in account. Difference in names at both places increases unwarranted confusion. Moreover, the auditor should seek help from the bank's IT Dept. for generation of reports based on difference in name as per CUST ID and as per accounts opened (if any).

(ii) Account Level Configurations

- (a) Configurations/ parameters for are set up at the time of Account Opening. Modification afterwards is also permitted. Account Level masters contain the parameters and details specifically with respect to account. For instance, Interest Rate, Interest payment periodicity, Freeze, Lien, etc.
- (b) It is important to note here that under CBS majority of functions and transactions are master driven and hence, any minor error at Master Level (whether Customer Master or Account Master) can have a

magnanimous effect on transaction processing. For e.g., if Interest Collection Flag is selected as "N" at Account Master Level, the system will not collect any interest. Hence, accuracy of master is a vital audit area.

(iii) Pointing Type Accounts/ Self Reconciling Accounts

- (a) Apart from maintaining customer accounts, the bank's general ledger also contains various Suspense/ Sundry Accounts.
- (b) Such accounts can be with debit or credit balance.
- (c) The said accounts are used for limited purposes and for parking of entries for limited time frame.
- (d) Transactions wherein either debit/ credit leg is not confirmed/ identifiable at the time of transactions are parked in such accounts. For e.g., an amount of Rs. 1,000 is given to an employee in advance for the purchase of stationery items for the branch. The said transaction will be kept under such Suspense/ Sundry account till the date the employee submits the bill/ returns the advance.
- (e) The transactions processed in such accounts are not routine hence it calls for continuous monitoring and earliest reversal.
- (f) Moreover, numerous transactions in an office account make it difficult for reconciliation.
- (g) In earlier times, the activity of reconciling the office account was manual.
- (h) However, under CBS such accounts are opened under Pointing Type Office Account/ Self Reconciling Accounts Scheme Code which facilitates automatic reconciliation and real-time information on outstanding/ non- reversed transactions.
- (i) Transactions in such types of accounts are in two parts - Originating Transaction and Reversal Transaction.
- (j) For each reversal entry, the system will prompt the user to point it to an originating transaction.
- (k) There can be multiple reversals against single originating transactions. Such type of account will also ensure that in case of a debit type office account, credit entry as originating entry will not be permitted.

- (l) On the user's side, at the time of reversal of Transaction the system will ask the user to "Point" the Originating Transaction against which the transaction is being reversed. On selection, the system will reduce the balance under the said Originating Transaction.
- (m) Under this type of Pointing Type Account, at any given point of time an aggregate of outstanding transaction-wise balance will be equal to the Office Account Ledger Balance.
- (n) Under Finacle, verification of outstanding/ non-reversed entries can be verified from menu command **IOT (Inquire on Transaction)**.
- (o) Moreover, a report on outstanding office account transactions can be generated through Menu **MSGOIRP**.
- (p) Various customized reports for the said purpose are also available under each banks "Report" menu in Finacle.
- (q) Under Bance, the outstanding entries are available through offline reports viz. "Audit BGL accounts age wise break up" and "GL-Outstanding-Accounts" report.
- (iv) **Interest in Table Maintenance**
 - (a) Interest collection as well as payment in CBS can be through Interest Tables or can be by way of absolute rate.
 - (b) In case a loan account wherein Interest Rate is based on a reference rate (say Base Rate), the Interest Rate field is updated with the Reference Rate Table to ensure automatic updating of Interest on subsequent change.
 - (c) In case of Interest Table master, the primary rate is sourced from a Master Table.
 - (d) For instance, in case of Loan sanctioned as Base Rate + 3% whereas Base Rate at the time of Sanction was 10%, the Interest Rate field will be updated either with BR+3 Table code or with BR Table with 3% updated in Account Preferential Debit Interest with +3%. The method of updating of interest may differ from bank to bank.
 - (e) In the case of a few specialized products (e.g., subsidy-linked accounts) a limit level interest rate is required to be applied.

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- (f) In such cases the parameters are set up at Interest Table Master Level and the said table code is updated under Interest Table field at Account Master Level.
- (g) In the case of a fixed rate loan, the interest rate is updated as an absolute figure in the Interest Rate field instead of Table. However, few banks follow the practice of updating “ZERO Interest Rate Table” with necessary interest rate at Account Preferential Debit Interest.
- (v) **Interest Flags**
 - (a) Values at Interest Flags determine the payment and collection of Interest.
 - (b) Applicable flags (i.e., Interest payment, Interest collection) are required to be updated at Account Master Level.
 - (c) Hence, if the Interest Collection Flag is updated as “N”, there will not be charging of interest by system, although proper Interest Table Master is selected.
- (vi) **Withholding Tax Flags**
 - (a) Interest payment to the customer is aggregated at Customer Master Level (i.e., for all the accounts opened under a CUST ID / CIF No.).
 - (b) The threshold limit for TDS is computed based on the amount aggregated at CUST ID Level.
 - (c) Once the payment of Interest exceeds the minimum threshold level prescribed under Income Tax provisions, the system initiates deduction of taxes from Interest.
 - (d) However, for cases wherein customer has submitted Form 15H/ 15G/ tax exemption certificate, necessary flags are required to be updated to prevent deduction of taxes up to the enhanced limit (as applicable).
 - (e) Even though Form 15H/15G certificates have been submitted to the Bank, when the threshold limit of TDS on interest exceeds, automatically the system has started to deduct TDS from 1st April and not from the date when the interest limit exceeds the threshold limit.
 - (f) Withholding Tax flags are available at both CUST ID and Account Master Level.

- (g) With the recent change in the Income Tax guidelines w.r.t. online submission of details of Form 15G/15H, the exemption is required to be flagged at CUST ID level for Interest Income declared by the customer.
- (h) In Finacle, withholding (TDS) flags are driven by Tax Slab. For each type of customer different tax slabs have been defined at Master Level e.g., TDS for individuals, TDS for corporations, TDS for exempt entities. It is important for the auditor to verify correctness of Tax Slab vis a vis constitution of customer.

(vii) Freezing Flags (Debit, Credit and Total)

- (a) In case of court order, dispute between the joint account holders, recovery notice from revenue authority the transactions in accounts are required to be suspended.
- (b) Depending upon the requirement the transactions are suspended (viz. Debit, Credit or all) through Freeze Flags.
- (c) The freeze can be applied at CUST ID Level (i.e., all the accounts of the customer) or specific accounts of the customer.
- (d) The source documents are required to be verified for marking of freeze and unfreeze event.
- (e) The inquiry of accounts with Freeze Flag can be made in Finacle through HACS Menu Command with Freeze Flag as "T" =Total Freeze, "D" =Debit Freeze, "C" =Credit Freeze.

(viii) Schemes and Scheme Codes

- (a) Different types of accounting products are offered to customers with different characteristics.
- (b) For instance, various types of Savings Accounts are offered. The aggregation of account balance for such cases will take place at Sub GL & GL Level. However, for account operations and account master setup different schemes are set up in CBS.
- (c) Scheme Code acts as a placeholder.
- (d) Inquiry for different types of accounts can be made in Finacle through ACS Menu Command with "Scheme Code".

Exception Types

The transaction errors are handled in CBS through following modes:

- a. Warning – Warns user for possible errors based on prefixed criteria.
- b. Exception – Allows user (with sufficient power) to override. However, the transaction will be recorded in Exception Report for the day.
- c. Error – Does not allow user to proceed further, unless the correct values are filled in.

Maker and Checker Matrix for Valid Transaction

- (a) Under CBS the transactions are processed by at least two officials of the bank under Maker and Checker mode.
- (b) The same is tracked through the transaction events (viz. entry, posting and verification).
- (c) Posting is the event which updates the GL Balance. Posting activity depends on the rights assigned to each user ID.

Inventory Locations

- (a) The inventory concept under CBS refers to handling of security stationeries, viz., non-personalized cheque books, Demand Drafts, Term Deposit Receipts.
- (b) Each bank, as per the requirement, creates different inventory location and inventory sub location codes in CBS.
- (c) Predominantly, locations are created for joint custody (dual custody), employee custody, external locations. Barring, external location, balancing of security stationery is available for all the locations.
- (d) In Finacle the report on outstanding inventory items can be generated through Menu command ISRA. Whereas under Bancs the same set of reports can be generated through VPIS (Valuable Paper Inventory System) module.

Zones in Clearing Modules

- (a) For easy identification of type of cheque and proper reconciliation various zones are opened on daily basis (as per clearing cycle) in CBS.

- (b) Various zones are opened for Non-CTS Cheques, Inter-bank Cheque, KYC Cheques, MICR Cheques, Non-MICR Cheques, Warrants, CMS Cheques, etc.
- (c) Opening of Zone is the primary event before lodging any Inward Clearing instrument or Outward Clearing Instrument.

Limit and Limit Node

- (a) Under Finacle the Limit Management is done through Limit Node Maintenance.
- (b) Wherein, the limits are specified at each node level with capping.
- (c) Credit Limits can be set at Account Level as well as at Node Level for deriving the Drawing Power for a customer.
- (d) Setting up of Limit at Node level has following advantages:
 - Managing two or more accounts with drawing power deriving from the same security.
 - Interchangeability of limits among different accounts.
 - Monitoring the overall exposure to a single client/ group of clients.
 - Exposure to a select commodity/ security. *Limit Node Maintenance* helps to build these requirements in the limit management.

Limit Node

- (a) Limit nodes are used to group accounts under one node to enable easy monitoring and organization.
- (b) A limit node can be linked to a security for deriving drawing power.
- (c) Distribution of overall group (group may be a group of clients or a group of accounts) limits to individual members (members may be accounts or clients) is possible through creation of Parent Node and Child Nodes.
- (d) Every child node can further be distributed to group of accounts or clients. This is diagrammatically explained through below example.

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Facility Type	Particulars	Limit (Rs. Lacs)	Remarks
Funded	Term Loan	225	Funded Limit Cap is 500 Lacs <i>Upper Limits fixed in each type of Facility</i>
	WCDL	75	
	CC	200	
	BP / FBP / BD	50	
Total Funded Facilities		500	
Non-Funded	LC	300	Non-Funded capping is at Rs. 500 Lacs
	BG	300	
Total Non-Funded Facilities		500	
Total Company Exposure		1000	Total Exposure to Company should not exceed 1,000 Lacs

Temporary Overdraft (TOD) Setup

Granting of TOD to a customer is a credit decision from bank's perspective. Concurrent auditor must review the source documents and delegated powers to ascertain whether the sanction was in line with the guidelines prescribed by the bank. Setup of TOD is done in Finacle as follows. TOD is granted to an account under various circumstances. For instance:

Type	Event	Mode
TODIC	Interest Calculation	Single
TODDL	Drop in Limit	Single
TODMN / TODUG	Manual / User Generated	Single/ Running/ Ad hoc

Explanation of various TOD modes is as follows.

Mode	Narrative
Single (S)	It refers to TOD for specific purpose/ transaction. It can be used only for the specific transaction during which the same was granted.

Running (R)	It refers to setting up a parallel limit at account level for a defined period over and above credit limits (if any).
Ad hoc (A)	Ad hoc allows customers with OD / CC Accounts to operate within TOD Limits for a defined period.

- (a) From above narrative it appears that running and ad hoc TODs serve the same purpose.
- (b) However, from CBS perspective, both the events are different. In case of single and running TOD, CBS computes the number of TOD sanctioned in the account.
- (c) In case the cumulative number exceeds the prescribed limit for an account, an exception gets triggered for all subsequent transactions.
- (d) Whereas in case of ad hoc TOD the said TOD is not counted under number of TODs thereby circumventing the exception controls embedded in the system.
- (e) It is important for auditors to verify cases wherein ad hoc Limits have not been delinked on expiry in system.

Register Type and Subtype (Trade Transactions)

- (a) The concept of Register Type and Sub Type is same as Transaction Type and sub types as discussed above.
- (b) The types are used to aggregate transactions of same nature in system.
- (c) It helps in identifying and tracking of transaction in a better manner.
- (d) In Finacle, Register Type and Sub Types have been used in Inland Trade Transaction and Foreign Trade Transactions modules.

List of few Register Types and Subtypes for an Import Transactions is as follows:

Reg. Type	Sub Type
Import Bill on Collection	Sight
Import Bill on Collection	Usance
Import Bill under LC	Sight
Import Bill under LC	Usance

Direct Import Bill	TT (Telegraphic Transfer) / DD (Foreign Demand Draft)
Advance Remittance against Import	TT (Telegraphic Transfer) / DD (Foreign Demand Draft)

Auditing through CBS

Generally, the following set of steps is recommended at the start of the audit to understand the operations at the branch level and familiarize oneself with the branch and its team:

- (a) Document list of software's, applications and interface details associated with CBS.
- (b) Review Usage Manual or Document Software navigation options and Menu Codes.
- (c) Document list of Reports available in CBS and its menu codes.
- (d) Review Exception Reports/ MIS Reports generated by Data Centre.
- (e) Review access rights, limited access and free access.

Parameters Affecting Automatic Identification of NPAs and Re-designing of Audit Processes

- (a) In terms of directives issued by Ministry of Finance and Reserve Bank of India, it is mandatory for banks to identify the bad loans through CBS/ Systems instead of conventional methods.
- (b) CBS like other software work on GIGO principle.
- (c) Master Data play an important role in correct identification of Bad Loans.

The following are a few scenarios wherein incorrect updating in Master Data, manipulation through transactions etc. may impact correct identification of bad loans through CBS.

Parameters	Auditors' Primary Checks	Suggested System Support
Discrepancies in setting up the EMI	Whether EMI/ instalment is correctly set up.	Finacle: – ACI -> Option "E" Repayment details

Core Banking System

/ Instalments	<p>Whether EMI/ instalment amount matches with the sanctioned terms.</p> <p>Whether periodicity of Instalment is correctly classified as per Sanctioned Terms?</p>	<p>Bancs:</p> <ul style="list-style-type: none"> - DL/TL Accounts & Services → Enquiries → Account - Deposit / CC / OD Accounts & Services → Enquiries → Deposit / CC/OD Account <p>(Short & Long Inquiry options are available under both menus.)</p>
<p>System determined Asset Classification vis a vis User defined Asset Classification</p>	<p>a. CBS contains two sets of parameters. At first instance CBS identify the account based on set parameters under A set Classification types.</p>	<p>Finacle:</p> <p>a. an ACM/ ACI Option – ‘Y’ Asset Classification Inquiry</p> <p>b. A report containing accounts wherein there is difference between Asset Classification by System and by user should be requested for. Accounts listed in the said report should be thoroughly verified.</p>
	<p>b. In a few CBS it has been observed the user is generally given the option to differ and select/ amend the classification. In such cases detailed scrutiny of the NPA system is required to be carried out.</p> <p>Due to errors in certain Master Data, there can be</p>	

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		erroneous identification of accounts as NPA. However, such accounts require detailed scrutiny.	
Manipulation in SL / DP	A	Changes in SL / DP should be cross checked with Sanctioned Letter.	Finacle: a ACLHM – Account Limit History Maintenance Bancs: a Tailor-made report on Changes in Account Limits
	B	Whether any change supported by necessary documentation?	
Incorrect moratorium period	A	Based on moratorium period CBS will identify the Loan Instalment and will track repayment.	Finacle: a ACI – Option “E” – Repayment Details Bancs: a. Account Master details (Long Inquiry)
	B	In case the moratorium period / instalment start date is erroneously updated system will not show correct result.	
Re-placement without reporting it as reschedule	A	Loan Account Instalments are rephrased / recalibrated without reporting the same as Re-schedule.	Finacle: a ACI – Option “E” – Repayment Details Bancs: Account Master details (Long Inquiry) b Report containing details of all the cases wherein EMI / Instalment is changed should be sought
	B	Verify whether any change in Repayment	

Core Banking System

	instruction is made through System. Compare the said accounts with list of Restructured	
	Accounts.	
Instalment Start Date is Future Date	a) Check whether the Instalment Start Date entered as per sanctioned term?	Finacle: a ACI – Option “E” – Repayment Details Bancs: Account Master details (Long Inquiry)
	b) In the case of a future date the system will not identify instalment, and any repayment received will be shown as “Overflow”.	
Interest Demand date (Future Date)	a Check whether Interest Start Date entered as per Sanctioned Term? b in case of future date as Interest Demand Date system will not accrue interest and any repayment received will be shown as “Overflow”.	Finacle: a ACI – Option “E” – Repayment Details Bancs: Account Master details (Long Inquiry)
Fictitious credit through Office Account / Inter- branch Account	a Are there any quarter/year-end credits cited in the account? b Check the source of Credit Entries. c Review transactions in Office Accounts/	Finacle: a. ACLI – (Use CTRL + E to Explore the Tran) b. Review of Office Account Ledgers Bancs: a Deposit / CC / OD Accounts &

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	Inter Branch Accounts.	Services → Enquiries → Transaction b. DL/TL Accounts & Services → Enquiries → Transaction
Round tripping from internal accounts	a Close scrutiny of transaction and review of chain/ series of transactions for accounts with deficiency is required. b Such transactions will inflate the Credit Turnover in the account.	Finacle: a ACLI – (Use CTRL + E to Explore the Tran) b Using only Account Turnover Information generated through “ATOR” / “CUTI” / “ACTI” menu may lead to incorrect inference, since the credits are not solitary credits in account. Bancs: a Deposit / CC / OD Accounts & Services → Enquiries → Transaction b DL/TL Accounts & Services → Enquiries → Transaction
Temporary Overdrafts	a Check whether the TOD is sanctioned to bring the overdrawn limit to base level additional facility through TOD is sanctioned.	Finacle: a ACLI – Option “O” b TODRP – TOD Register Printing Bancs: TOD Report
Devolved bills parked in Office Accounts and	a Devolved Bills under LCs are required to be debited to the Limit Accounts only.	Finacle: a BI & FBI – with Bill Status as “K” using status date filter.

Core Banking System

not in limit account	<p>Assessment of Asset Classification will be based on composite overdrawn portion Limit + LC Devolved amount (if any on devolvement)</p> <p>b Check whether the amount of devolvement of LC backed bills are parked in Office Accounts or any separate account?</p>	<p>Bancs:</p> <p>Report on Devolved bills under Import LC</p>
Multiple CUST ID to prevent the other account from becoming NPA	<p>a Check whether multiple CUST IDs have been opened for the borrower with different accounts?</p> <p>b NPA Report and search all the case by few characters of Name.</p>	<p>Finacle:</p> <p>a ACS – Account Selection (Search based on Name)</p> <p>b LAGI – Loan Account General Inquiry (Inquiry based on other parameters)</p> <p>Bancs:</p> <p>a. Customer Management → Enquiries → Search by Name</p>

Parameters Affecting Collection of Interest/ Revenue

- (a) Primary revenue for banks is interest on loans and advances. Charging of interest is completely automated barring few products.
- (b) However, the processing is based on certain important parameters. System parameters / fields which affect the interest computation should be thoroughly verified.
- (c) Some important interest parameters are as follows:
 - (i) Interest Table.

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- Debit Interest Rate and Credit Interest Rate.
 - Interest Version.
 - Currency.
 - Limit Level Interest.
- Penal charges.
- (ii) Interest Rate (Static/Absolute and Based on Ref. Rate).
- (iii) Interest Preferential Customer Level - Interest rate preference will be applied to all the accounts of the customer based on type of Interest.
 - Debit Interest Preferential.
 - Positive preference value
 - Negative preference value
 - Credit Interest Preferential.
 - Positive preference value
 - Negative preference value
- (iv) Interest Preferential Account Level - Interest rate preference will be applied to the specific account wherein the preference is updated.
 - Debit Interest Preferential.
 - Positive preference value
 - Negative preference value
 - Credit Interest Preferential.
 - Positive preference value
 - Negative preference value
- (v) System Support / Important Menu Codes:
 - Finacle: INTCL, AINTRPT, INTPRF, INTTM
 - TCS Bancs: i) OD/CC Accounts -> Interest Rate History ii) DL / TL-> Interest Rate History

Following are few events/ scenarios wherein there is a possibility of non-application/ incorrect application of Interest:

Sr. No.	Event / Scenario
1	Interest pegging in Advance Accounts set as "Y". (If "Y" is selected, system will charge interest at the rate prevailing at the time of Account Opening. For the cases of Fixed Rate Loans Pegging Flag will be "Y")
2	Future Date is updated in Interest Demand Date
3	Interest on Principal / Payment of Interest Flag is set as "N"
4	Effective Rate of Interest is updated as "0"
5	Account Open and Instalment Start Dates are identical
6	Account Open and Interest Demand Dates are identical
7	Interest Table Code "Zero" is selected
8	Interest Demand Date is Past Date
9	Interest Demand Frequency is Blank

Audit of Foreign Exchange Transactions with the Use of CBS

The liberalization of economy is paving way for opening of new areas for inbound and outbound investment. Moreover, with the increase in the global trade the foreign exchange and cross border transactions are increasing at a rapid speed. However, it also poses challenge of preventing misuse of regulations and money laundering activities.

Following are few activities that the auditor must carry out for concurrent audit of Foreign Exchange Transactions:

Audit Activity	Important Menu Codes of Finacle
Review of Letter of Credits issued,	For Inquiry – DCQRY
Expired, Search on Outstanding LCs	For Report – DCREG, DCRPTS, DCSTMT

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Review of Bank Guarantee issued, invoked, closed, outstanding, Search on expired BGs	For Inquiry – GI For Report – GILR, GPI
Audit of Inland Bills (under collection, under LC, discounted)	For search: BI Search result printing: BP For specific bill: BM
Audit of outstanding Inland Bills	Report – BRGR (Collection Bills), BRBPR (Purchased Bills)
Audit of Foreign Bills (under collection, under LC, discounted)	For search: FBI Search result printing: FBP For specific bill: FBM
Audit of outstanding Foreign Bills	Report – FBBR
Audit for Inward and Outward Remittances (Other than Import and Export Transactions)	For Inward Remittance: IRM For Outward Remittance: ORM
Tracking of Packing Credit granted and tracking of order in case of Running Packing Credit	Account wise Packing Credit: ACLI Running Packing Credit: RPCTM

Audit of Office Account Transactions through CBS

- (a) Office accounts are opened for the purpose of parking entries till the time the final effect is not determined.
- (b) However, at various occasions it has been observed that the entries remain in the said parking accounts for a long period.
- (c) Moreover, in case of weak monitoring of the said accounts, the Office Accounts are susceptible to fraud and misappropriation.
- (d) There are various types of office accounts:
 - (i) Based on Functionality:
 - Pointing Type/ Self Reconciling Accounts.
 - Non-Pointing Type Accounts.
 - Based on Type of Entry Sundry Accounts, Suspense Accounts.
 - EOD/BOD Check Accounts.

Core Banking System

- Inter branch Account.
- Mirror Accounts.
- Pool Accounts.

Following are few audits actionable for concurrent auditor carrying out audit of Office Account Transactions:

Events	Audit actionable	Suggested system support
Cash Payment from Office Accounts	Authorization of Transaction as per Delegated Authority	Finacle: <ul style="list-style-type: none"> • ACLI – For Transaction • FTI – For Search Bancs: <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction
TOD through Office Accounts	<p>Through ineligible credit originating from an office account, customers can be accommodated.</p> <p>It also circumvents the number of TODs granted to customers.</p> <p>Moreover, interest will not be applied in the said case.</p>	Finacle: <ul style="list-style-type: none"> • ACLI – For Transaction in Office Account Bancs: <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction
Parking of Cash Difference in Office Accounts, Clearing/Remittance differences through Office Accounts	<p>Difference in Reconciliation, Cash Shortage debited to Office Account and not reversed.</p> <p>Review ledger accounts in detail on a monthly basis.</p>	Finacle: <ul style="list-style-type: none"> • ACLI – For Transaction in Office Account • IOT – For inquiry on outstanding transaction • MSGOIRP – For

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		<p>Printing of outstanding office account transaction report</p> <p>Bancs:</p> <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction. • "Outstanding BGL Transaction" Report
Rotation of entries in Office Accounts	<p>To prevent entry being reported as long outstanding entry, a new transaction with debit and credit leg in the same account is posted. Thus, the system considers the new transaction date for reporting as outstanding entries.</p> <p>Review transactions with same Debit and Credit amount through Ledger Scrutiny</p>	<p>Finacle:</p> <ul style="list-style-type: none"> • ACLI – For Transaction in Office Account <p>Bancs:</p> <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction
Correctness in mapping of reversal transaction to originating transaction	<p>If the transactions have not been reversed against the related originating entries the report generated by CBS will show incorrect outstanding items.</p>	<p>Finacle:</p> <ul style="list-style-type: none"> • ACLI – For Reversal Transaction in Office Account <p>Bancs:</p> <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction
Value Dated (Back Dated) Transactions	<p>Transaction credited in the advanced type accounts, Operative accounts with a value</p>	<p>Finacle:</p> <ul style="list-style-type: none"> • ACLI – For Transaction in Office Account

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	<p>date (Back date) wherein the clear funds were not available in the office accounts.</p> <p>Review of the transactions from Revenue Leakage perspective.</p>	<ul style="list-style-type: none"> • FTI – For Value Dated Transaction <p>Bancs:</p> <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction
Round Tripping	<p>Rotation of entry from office account to operative account(s) without any justification/ source document.</p> <p>Review the transactions from the perspective of inflating credit turnover of account.</p>	<p>Finacle:</p> <ul style="list-style-type: none"> • ACLI – For Transaction in Office Account <p>Bancs:</p> <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction
Advance paid for Fixed Assets not capitalized	<p>Entries for payment of advance against procurement of Fixed Assets not reversed.</p>	<p>Finacle:</p> <ul style="list-style-type: none"> • ACLI – For Transaction in Office Account • IOT – For inquiry on outstanding transaction • MSGOIRP – For Printing of outstanding office account transaction report
		<p>Bancs:</p> <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction. • “Outstanding BGL

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		Transaction” Report
Income realized not credited to Revenue Account	Loan Instalment received from Customer, not adjusted. Processing Fees received, not credited to Income Account Charges collected, not credit to Income Account	Finacle: <ul style="list-style-type: none"> • ACLI – For Transaction in Office Account • IOT – For inquiry on outstanding transaction • MSGOIRP – For Printing of outstanding office account transaction report
		Bancs: <ul style="list-style-type: none"> • BGL -> Enquire -> Transaction • “Outstanding BGL Transaction” Report

Manual Updating in CBS and its Verification Aspects

- Under any CBS the transactions are processed as per pre-defined process.
- Majority of the processes in CBS are automated and based on masters.
- A manual intervention in automated process leads to error in transaction processing. Following are few manual changes/modifications in system which affects the transaction processing.
- The concurrent auditor must review the manual updating in CBS on monthly basis:

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Manual Entry	Probable impact
Advances	
Interest Rate change	Revenue Leakage, Excess collection of Interest
Change in EMI	Revenue Leakage, NPA Identification
Processing of transactions against un- cleared outward clearing effect	Recovery of amount from customer in case of cheque return
Backdated Renewal Date updating (Updating Date of Renewal on running date with past date)	NPA Identification
Change in Limit – From Non-Fund Base to Fund Base	NPA Identification
Manual entry for adjustment of recovery in NPA	Incorrect NPA update in principal / Interest
Account & Customer Master	
Tax exemption update	Non-compliance with TDS provisions
Dormant to Active	Susceptible to fraud
Interest Table Code as “0”	Revenue Leakage
Interest Collection Flag “N”	Revenue Leakage
Reclassification of Agriculture Advance as per revised RBI norms dt. April 23, 2015	Sectorial Classification
Foreign Exchange Transactions	
Erroneous Foreign Exchange Rate	Revenue Leakage, Accommodation to customer
Full BOE received flag marked as “Y” wherein BOE for entire transaction is not received	Reporting to RBI under BEF Return
FIRC Issuance (without updating flag printed “Y”)	Duplicate issuance of FIRC without “Duplicate FIRC” inscription.

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Merchant Trade Transaction (Manual mapping)	Reporting to RBI
Transaction Processing & Housekeeping	
Changes / Modification in Auto Calculated charge amount at the time of posting of transaction	Revenue Leakage
Ineligible Credits to NRE and FCRA Accounts	Non-compliance of FEMA Guidelines
ATM Replenishment entries	Susceptible to Fraud
Payment for FD Closure proceeds in Cash through Office Accounts more than ` 20,000	Non-compliance with Income Tax Guidelines
Revalidation of Old DDs	Susceptible to Fraud
Value Dating (Credit Transactions in CC / OD Account with Value Date without Value Dating at Debit Leg)	Revenue Leakage
Debit to Income Account (though Transaction Maintenance Menu)	Revenue Leakage
Manual Credit to Income Account (though Transaction Maintenance Menu)	Revenue Leakage (Computation of Income credited to be verified)
RTGS / NEFT in cash through office accounts > 49,999	Non-compliance with AML guidelines
Delay in posting of clearing cheque return	Accommodation to customer
Manual Transfer of Security Stationery from Inventory location to External Location	Susceptible to Fraud (Avoid reporting of missing inventory)

Generation and Verification of Specific Reports Based on Various Criteria

CBS allows generation of various reports through frontend as well as through backend. Few important reports for review by concurrent auditors are as follows:

(a) Exception Report

Reports for the month end and two days prior and after the month end should be verified. Exceptions of the following nature should be closely verified:

- (i) Balance exceeded Account Limit.
- (ii) Manual debits to Income Account.
- (iii) Value Dated Transactions.
- (iv) Manual entry for SI Failure cases.
- (v) Instrument passed against Clearing.
- (vi) Backdated entries (normally restricted).

(b) Irregularity Report

Reports for the month end and two days prior and after the month end should be verified. Report contains details of Accounts where Balance in Accounts are greater than the limits sanctioned. Check whether the same is due to:

- (i) Application of Interest.
- (ii) Granting of Intra Day TOD.
- (iii) Passing of Instruments against Clearing Effects.

(c) Accounts where Interest Code is '0'

Interest will not be charged from Accounts where Interest Code is selected as '0'. Hence, a detailed check is required. Possible reasons can be if it is an NPA account or an account with a moratorium.

(d) Interest Collection Flag as "No"

If Interest Collection Flag is selected as "No", Software will not consider the account for calculation and entry for Debit Interest.

(e) Debit Interest SI Failed Report

1. Failure of Standing Instruction for Debit Interest should be closely verified. If the SI is failed, the Account will not be debited for Interest. SI Failure can be for any reason like:
 - (i) Non-availability of Balance in Account (In case of TOD in Operative Account).
 - (ii) Non-availability of Limit in Account.
 - (iii) Technical Snag in execution.

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2. Whether the Branch has manually passed the entry for all such cases should be verified.

(f) Loan Instalment SI Failed Report

Same as above.

(g) Report containing all Advance Accounts with Limits

Generally, CBS Software's generate a Report wherein details of all Advance Accounts are listed. Excel can be used to verify cases of DP > SL, Margin Requirement, etc.

(h) TOD Report

Documents and sanction orders should be verified for all the cases of Manually granted TODs. In Finacle the report can be generated through Menu Code "TODRP".

(i) Account Turnover Report

To review the quantum of transactions in the borrower accounts, turnover reports should be used. In Finacle, inquiry for Account Turnover can be carried out through "ACTI, CUTI" Menu codes and report can be generated through "ATOR" Menu.

(j) Loan Inquiry

In Finacle, criterion-based search for Loan Accounts is available through Menu option "LAGI". The said menu can be used to verify:

- New sanction, Accounts closed.
- Loans under various schemes.
- Loans based on Account Classifications.
- Accounts search based on Limit (Credit & Stock Audit).

(k) Loan Overdue Inquiry

In Finacle, criterion-based search for Overdue & Overflow Loan Accounts is available through Menu option "LAOPI". In case of Bancs the said details are available through an offline daily report. The said menu can be used to verify:

- Principle & Interest Overdue and Overflow.
- Overdue in "%" as well as Overdue in "No. of Days".

(II) Financial Transaction Inquiry

In Finacle, report based on different criteria for financial transactions can be generated through Menu Option “FTR”. The said menu can be used to verify:

- Loan disbursement in Cash (Sub GL code & Tran Type).
- Value Dated Transactions verification (Only value dated flag).
- Transactions in Loan / OD-CC Accounts (Sub GL, Tran Type, Part Tran Type).
- Credits to NRE Accounts in a period (Sub GL, Part Tran Type).
- Credits to FCRA Accounts in a period (Sub GL, Part Tran Type).
- Cash Deposit Transactions above Rs. 50,000 to verify compliance with Income Tax Guidelines on PAN (Tran Type, Tran Sub Type).
- Cash Transactions above Rs. 10 Lacs to verify compliance with AML Guidelines (Tran Type).
- Debits to ESCROW Accounts to verify compliance with ESCROW Agreement (Sub GL, Part Tran Type).

Guide on Audit Activity through CBS for LFAR and Tax Audit Requirements

- (a) Each bank uses its own format for concurrent audits.
- (b) A common report format used by all the banks is of Long Form Audit Report (issued by statutory auditor).
- (c) Following are few checkpoints for concurrent auditors along with suggested system support.

Audit Activity / Process / Audit Area	Auditors' Primary Checks	Suggested System Support
Cash	D Physical verification of Cash Balance D Cash Balance as on the date of Audit Period D Cash Balances reported in Friday	Finacle: D “ACLI” - Account Ledger Inquiry (Vault A/c and Teller Accounts) Bancs: D → Reports → Cash Related View Cash

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	Statement	<p>Summary (Click on Fetch)</p> <p>D → Branch Reports → Cash Officer's Jotting Book Report</p> <p>D → Reports → Printing Reports → Cashier / Teller Cash Report</p>
Balances with RBI / SBI / Other Banks	<p>D Balance as on Date</p> <p>D Transactions in Mirror Accounts</p> <p>D Reconciliation Statement (Generally outside of CBS)</p>	<p>Finacle:</p> <p>D "ACLI" - Account Ledger Inquiry</p> <p>Bancs:</p> <p>D → Branch Accounting (BGL) → Enquire → Transaction</p>
Advances	D Sanction Limit / Drawing Power setup	<p>Finacle:</p> <p>D "ACLHM" – Account Limit History Maintenance</p> <p>D "ACM / ACI" – Account Master (Go to Limit details)</p> <p>D "LTL" – Limit Tree Lookup (Tree views of all Limits)</p>
Advances	<p>D Account & Customer Master parameters setup viz.,</p> <p>D Interest Parameters (Regular & Penal charges)</p> <p>D Repayment Instructions</p> <p>D Standing Instructions (SI) Parameters</p>	<p>Finacle:</p> <p>D "ACLHM" – Account Limit History Maintenance for DP & SL – Account Specific</p> <p>D "ACM / ACI" – Account Master</p> <p>D "CUMM / CUMI" – Customer Master</p> <p>Bancs:</p> <p>D DL/TL Accounts & Services → Enquiries → Account</p> <p>D Deposit / CC / OD Accounts & Services → Enquiries → Deposit / CC / OD Account</p> <p>(Short & Long Inquiry)</p>

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		<i>options are available under both menus.)</i>
Advances	D Transactions in Borrower's Account	Finacle: D "ACLI" - Account Ledger Inquiry Bancs: D Deposit / CC / OD Accounts & Services → Enquiries → Transaction D DL/TL Accounts & Services → Enquiries → Transaction
Advances	D Interest Rate History	Finacle: D "INTTM" – Interest Table Master Maintenance (Under Inquire Mode – Account Specific) Bancs: D Deposit / CC / OD Accounts & Services → Interest Rate History D DL/TL Accounts & Services → Interest Rate History
Advances	D Conduct of Account and Credit Turnover D Turnover of CC Account based on Borrower's Business profile D In case of Loan accounts ACTUAL recovery of Installments and Interest	Finacle: D "ATOR" – Account Turnover Report D "ACTI" – Account Turnover Inquiry D "CUTI" – Customer Level Turnover Inquiry Bancs: D DL / TL Accounts & Services → Enquiries → Long D Deposit/CC/OD Accounts & Services → Enquiries → Long

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Advances	D Non-Performing Asset D Search for an Account based on Criteria	Finacle: D “ ACS ” – Account Selection (2nd Screen – IRAC Code – Main Asset Classification)
		Bancs: D DL / TL Accounts & Services → Enquiries → Short → Select Option “1” – TL / DL [Long Inquiry for NPA Date] D Deposit/CC/OD Accounts & Services → Enquiries → Short → Select Option “2” – CC / OD [Long Inquiry for NPA Date] D Common Processing → Overdue / NPA → NPA Enquiry (Risk Grade Inquiry / NPA Status Inquiry)
Advances	D Interest Report	Finacle: D “ AINRPT ” – Interest Report for Account Bancs: D Product Sheets – To be requested from Data Center (if not available through user login)
Advances	D Primary & Collateral Security Maintenance	Finacle: D “ SRM ” – Security Register Maintenance Bancs: D DL/ TL Accounts & Services → Security (Primary/ Collateral) → Customer → Amend / Enquiry → Amend/ Enquire Security

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Advances	D Lien Marking	Finacle: D “ ALM ” – Account Lien Maintenance Bancs: D DL/ TL Accounts & Services → Security (Primary/ Collateral) → Customer → Amend / Enquiry → Amend / Enquire Security <i>(Under Bancs – Collateral ID is required to be created before setting up limits)</i>
Advances	D Account Printing Ledger	Finacle: D “ PSP ” – Pass Sheet Print D “ ACLPCA ” – Customer Ledger Account Print Bancs: D Print Menu available under DL / TL Accounts & Services and Deposit / CC / OD Accounts & Services
Advances	D Non-Fund based Facility (LC, BG)	Finacle: D “ GI ” – Guarantee Inquiry D “ DCQRY ” – Documentary Credit Query Bancs: D Report generated from Trade module
Stationery	D Physical Verification of Stationery and confirmation of Balance as per CBS	Finacle: D “ ISRA ” – Inventory Status Report (<i>Location wise viz., Dual Lock, Individual, Cancelled etc.</i>) Bancs: D Through Valuable Paper

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		Inventory System [VPIS] module
Office Accounts (Suspense, Sundry etc.)	D Outstanding entries for reporting D Entries outstanding Whether any Provisioning is required?	Finacle: D “ IOT ” – Inquire on Transaction (As on date Inquiry) D “ MSGOIRP ” – Outstanding Items Report Bancs: D Through offline reports viz. “Audit BGL accounts age wise break up” and “GL-Outstanding-Accounts” report.
Office Accounts (Suspense, Sundry etc.)	D Printing Office Accounts	Finacle: D “ ACLPOA ” – Account Ledger printing Office Account Bancs: D BGL Accounting Menu
Inter Branch Account	D Un-reconciled transactions	Finacle: D Through Outstanding IBR Report.
		Bancs: D Through offline “Outstanding IBR Report “ / “IBR Summary report”
TDS Related	D TDS Information and Reports	Finacle: D “ TDSIP ” – TDS Inquiry & Reports D Month-end report on account wise / transaction wise Tax deduction. D Bank specific customized Menu / report

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		Bancs: D Through offline monthly report on account wise / transaction wise Tax deduction.
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List of Important Menu Commands

Following is the list of various important menu commands for concurrent auditors based on area of operations in the bank:

(i) Accounts, Customer Master and Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	CUMM / CUMI	Customer Master Maintenance / Inquiry	Inquiry
Finacle 10	CRM Module	Customer Master maintenance	Inquiry & Modifications
Finacle 10	HACLI, HACLINQ	Account Ledger Inquiry	Inquiry
Finacle 10	HACM, HACMTD	Account Master, Account Master Term Deposits	Inquiry
Finacle 10	HINTTM	Interest in Table	Inquiry
Finacle 10	HAFI	Audit File Inquiry	Inquiry
Bancs	Customer Management → Enquiries → Search by CIF Number	To verify all accounts of one Customer	Inquiry

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Bancs	Customer Management → Enquiries → Search by ID Number	Search using available information (ID Number)	Inquiry
Bancs	Customer Management → Enquiries → Search by Name	Search using available information (Name)	Inquiry
Bancs	Customer Management → Relationship/Ownership → Associated Accounts	Inquiry on	Inquiry
Flex Cube	CH021	Account Master Maintenance	Inquiry
Flex Cube	CH701	Customer account balances-Other than loans-For standard accounts but including CC limit accounts	Inquiry
Flex Cube	CH703	RD account balances-Customer wise	Inquiry
Flex Cube	2000	CTI Customer Search	Inquiry
Flex Cube	7004	Customer Name	Inquiry
Flex Cube	7100	All Balance Inquiry	Inquiry
Flex Cube	7105	Display Customer Image	Inquiry

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Flex Cube	BA095	Account Level Attributes Inquiry	Inquiry
Flex Cube	7002	Balance Inquiry	Inquiry
Flex Cube	CH031	Statement Inquiry	Inquiry
Flex Cube	1337	TermDeposit	Inquiry
Flex Cube	7020	TERM DEPOSIT Balance Inquiry	Inquiry
Flex Cube	TD023	TERM DEPOSIT Rates History Inquiry	Inquiry
Flex Cube	TD031	TERM DEPOSIT Audit Trail Inquiry	Inquiry
Flex Cube	TD037	TERM DEPOSIT Account Ledger Inquiry	Inquiry
Flex Cube	TD050	TERM DEPOSIT Interest Inquiry	Inquiry
Flex Cube	TD11	TDS Inquiry	Inquiry

(ii) Transactions

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HTI	Transaction Maintenance / Inquiry	Inquiry
Finacle 10	HFTI	Financial Transaction Inquiry	Inquiry (Search / Criterion based)
Bancs	Deposit / CC / OD Accounts & Services	Transaction Enquiry (Additional	Inquiry

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	Enquiries → Transaction	options valuable: Transaction Types: 99 – All Financial, 98 – Cash Transaction, 25 – Repayment Details, 33 – Message Details	
Bancs	Branch Accounting (BGL) Enquire → Transaction	BGL Transaction Enquiry	Inquiry
Flex Cube	TD044	TD Transactions Inquiry	Inquiry
Flex Cube	LN058	Loan Interest Adjustment Transaction	Inquiry
Flex Cube	PM025	Payment Transaction Inquiry	Inquiry
Flex Cube	GLM04	GL Transactions and Movements Inquiry	Inquiry
Flex Cube	AT002	Audit Trail Financial Transactions Inquiry	Inquiry
Flex Cube	BA777	Audit Trail Inquiry for Non-Financial Txns	Inquiry

(iii) Clearing Transactions

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry /
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			Report)
Finacle 10	HOCTM	Maintain Clearing Zone	Inquiry
Finacle 10	HICTM	Outward Clearing Transaction Maintenance	Inquiry
Finacle 10	HMCLZOH	Inward Clearing Transaction Maintenance	Inquiry
Bancs	Collection and Cheque Purchase → Enquiries → Enquiries	Inquiry about Cheque Purchase / On Collection	Inquiry
Flex Cube	ST023	Outward Clearing	Inquiry
Flex Cube	ST033	Inward Clearing	Inquiry
Flex Cube	BA990	Clearing Inquiry	Inquiry
Flex Cube	ST002	Value Date Clearing Inquiry	Inquiry

(iv) Office Accounts Maintenance

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HIOT	Inquire on Transaction	Inquiry & Report
Finacle 10	HACLPOA	Account Ledger Print Office Account	Report
Bancs	→ Branch Accounting (BGL) →	Enquiry on BGL Account	Inquiry

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	Enquire → Account		
Bancs	→ Branch Accounting (BGL) → Enquire → Account Number Search	Search for an Account Number by BGL Name	Inquiry
Bancs	→ Branch Accounting (BGL) → Enquire → Transaction	BGL Transaction Enquiry	Inquiry
Flex Cube	GLM01	GL Voucher Entry	Inquiry
Flex Cube	GLM02	Chart of Accounts	Inquiry
Flex Cube	GLM04	GL Transactions	Inquiry
Flex Cube	1005	Miscellaneous GL Transfer (Dr/Cr)	Inquiry

(v) Loans & Advances

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HSCLM	Security	Inquiry
Finacle 10	HALM	Account Lien Maintenance	Inquiry
Finacle 10	HACTODM	Account TOD Maintenance	Inquiry
Finacle 10	HPSP	Pass Sheet Print	Report
Finacle 10	HACLHM	Account Limit	Inquiry

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Finacle 10	HAINTRPT	Interest Report for Accounts	Report
Finacle 10	HINTPRF	Interest Proof Report	Report
Bancs	Deposit / CC / OD Accounts & Services → Enquiries → Deposit / CC / OD Account	To verify the Account Master Details	Inquiry
Bancs	Deposit / CC / OD Accounts & Services → Enquiries → Statement Print	Printing Statement of Account for a Deposit or CC/ OD	Report
Bancs	Deposit / CC / OD Accounts & Services → Enquiries → Short	Basic details on Enquiry on Screen on Deposit Accounts	Inquiry
Bancs	Deposit / CC / OD Accounts & Services → Enquiries → Long	Additional Details on Enquiry Screen for Deposit Accounts	Inquiry
Bancs	Deposit / CC / OD Accounts & Services → Interest Rate History	Details of changes in Interest Rate for an account	Inquiry
Bancs	→ DL/TL Accounts & Services → Loan Tracking → Operations	Loan account operations	Inquiry

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Bancs	→ DL/TL Accounts & Services → Loan Processing → Generate Repayment Schedules → Action – “E”	To print Repayment schedule for a DL / TL Account	Report
Bancs	→ DL/TL Accounts & Services → Enquiries → Short Option “Balance Breakup Enquiry”	To view amount of Arrears & Breakup of Principal, Interest Realized, Charges & Arrear of Interest	Inquiry
Bancs	→ DL/TL Accounts & Services → Security (Primary / Collateral) → Customer → Enquiry → Enquire Security Summary	Enquire on linked collateral	Inquiry
Flex Cube	CH066	Limit Collateral Inquiry	Inquiry
Flex Cube	CHM06	OD Collateral Maintenance	Inquiry
Flex Cube	CHM07	OD Limit Master Maintenance	Inquiry
Flex Cube	ST070	Cheque Purchase	Inquiry

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Flex Cube	CH033	Average Quarterly / Monthly Balance Inquiry	Inquiry
Flex Cube	TDM24	Lien Master	Inquiry
Flex Cube	1413	Loan Disbursement Inquiry	Inquiry
Flex Cube	LN522	Account Schedule Inquiry	Inquiry
Flex Cube	LN10	Account Transactions Inquiry	Inquiry
Flex Cube	BA433	Collateral To Accounts Inquiry	Inquiry
Flex Cube	BA434	Account To Collateral Inquiry	Inquiry

(vi) DD/ PO, Cheque Book maintenance, Stop Payments and Security Stationery maintenance.

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HDDSM	DD Status Maintenance	Inquiry
Finacle 10	HDDIP	Inquiry on Specific DD Paid	Inquiry
Finacle 10	HISRA	Inventory Status Report	Report
Finacle 10	HIMI	Inventory Movement Inquiry	Inquiry
Finacle 10	HICHB	Issue Cheque Book	Inquiry

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Finacle 10	HCHBM	Cheque Book Maintenance	Inquiry
Finacle 10	HSPP	Stop Payment of Cheque	Inquiry
Finacle 10	HSPRG	Stop Payment Register	Inquiry
Bancs	→ Valuable Paper Inventory System [VPIS] → Enquiry of VPIS → General Enquiry	To check inventory status	Inquiry
Bancs	→ VPIS → Lost / Damaged Inventories	Location for Lost / Damaged / Cancelled Inventories	Inquiry
Bancs	→ VPIS Enquiry of VPIS → Teller Level Inquiry	Details of Inventory available at Teller level	Inquiry
Flex Cube	CH078	Cheque Status Maintenance	Inquiry
Flex Cube	CHM35	Stop Cheque Instructions	Inquiry
Flex Cube	CHM37	Cheque Book Issue Maintenance	Inquiry
Flex Cube	IV011	Stock Inquiry	Inquiry
Flex Cube	IV004	Inventory Lost report Register maintenance	Inquiry

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Flex Cube	MCA80	Inquiry about sold/issued inventory	Inquiry
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(vii) Compliances

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HTDSIP	TDS Inquiry / Print	Inquiry and Report
Finacle 10	HAFSM	Account Freeze Maintenance	Inquiry
Flex Cube	TDS06	Tax Parameters Maintenance	Inquiry
Flex Cube	TDS04	Tax waiver criteria Maintenance	Inquiry
Flex Cube	TDS05	Customer special Tax code maintenance	Inquiry
Flex Cube	TDS11	Tax Inquiry	Inquiry

(viii) Trade Finance and Foreign Exchange Transactions

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HINBOEM	Bill of Entry Maintenance	Inquiry
Finacle 10	MIIB	Maintain Import & Inward Bills	Inquiry
Finacle 10	MEOB	Maintain Export & Outward Bills	Inquiry
Finacle 10	IBL	Bill Inquiry	Inquiry

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			(Criterion based search)
Finacle 10	HBRBPR	Balancing Report for	Inquiry
Finacle 10	HBRCR	Balancing Report for Bills on Collection (Inland)	Inquiry
Finacle 10	HFBBR	Balancing Report for Foreign Bills	Inquiry
Finacle 10	HGI	Guarantee Inquiry	Inquiry
Finacle 10	HIRM	Inward Remittance Maintenance	Inquiry
Finacle 10	HORM	Outward Remittance Maintenance	Inquiry

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CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Flex Cube	SY001	Guarantee Inquiry	Inquiry
Flex Cube	BIM04	Bill Parameters Maintenance	Inquiry
Flex Cube	BIM05	Bills Processing Maintenance	Inquiry
Flex Cube	BI001	Bills Data Entry	Inquiry

Note:

1. The discussion of Menu codes / commands in this chapter is only for

guidance of members.

2. The purpose of inclusion of the same here is to understand the functioning of banking software.
3. Moreover, with the continuous changes and customization requests by banks, all the menu codes may not be available / accessible in all the banks.
4. The Finacle menu codes discussed in this chapter is for version 7 (except expressly mentioned).
5. Finacle has introduced a new version, namely Finacle 10.X. Few banks have already migrated to the newer version and few more are in process of migration.
6. Under Finacle 10.X there are changes in Menu Codes apart from other navigational changes.

Disclaimer:

1. Images, Logo, Screen Shots, Menu Codes, Software Name, etc., are the property of respective Software developers/ Trademark owners.
2. ICAI is not responsible for any violation of points mentioned in Para 1

Special consideration for Audit CBS Environment:

1. In the software, at the time of making provisions for interest rate accrued, only correct interest rate must be fed into the system. But few banks “rounds interest rate” instead of “rounding of interest amount”. This will create “Higher interest provision” or “Lower Interest Provision”. Auditors must certify the Profit/loss of the bank as “True and Fair View”. Hence the auditor must take proper due care of verification of this area at the end of every quarter/Half yearly/Annually.
2. In few banks, it is noticed that Interest paid on Reinvestment Deposit is on the Higher side. This means due to the mistake committed in the software programme, there are lot of scope for income leakage. The auditor must check all the Deposit (closed on time or at premature time) thoroughly so that there will not be any income leakage.
3. The auditor must see whether the system has got “reporting” style of “Legal cases pending at DRT/Notices sent to Defaulted Borrowers/ Decreed advance status” – Otherwise the comments must be passed by the Auditors on this ground.

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4. To avoid NPA, few Banks change the Master Records and change the due date to Next year. So, the system will not classify that advance as NPA. The auditor must be very careful to see the NPA working based on the Sanction letter terms and conditions and see whether there is any alteration in the Master records of the Bank or not.
5. Every day, the branch must close the “Day end process”. For every entry must be passed by the Clerk and the same must be approved by the Officer/Branch Manager. The system will allow the “Day End Process” only when every entry is approved. Sometimes some mischievous entries are passed in the system by other officials who are not directly related to the branch, say to avoid NPA at the Branch system (coming on deputation purposely). This passing of the entry is not known to any of the branch officials. At the “Day End Process” the system will not allow the branch to Close the Accounts, as the entries have not been approved by any branch officials. Normally the branch manager/officer must approve the “day end process” entries one by one. There is a system weakness in the Bank and the provision is for any untallied entries in the system, the concept of “Bulk approval” is there. The branch to close the “Day end Process”, give the approval under “Bulk approval” mode. This indirectly forced the Branch to approve all the “mischievous entries” without their knowledge. Hence the auditor must verify all the approval done by the Branch in the form of “Bulk approval” and satisfy himself before giving his report.
6. The unrectified entries in UPI transactions create lot of scope for fraud. Hence the auditor must verify the “reconciliation” of all those unrectified UPI transactions.
7. Kindly check the “Automatic Renewal” command of Deposits – whether the deposit is renewed only for the period mentioned in the Matured deposit or any other period the deposit is renewed.
8. In the Branch computerized system, to avoid NPA, money of other person is credited into the NPA account. On the same day or next day, the entry is reversed as “Wrong Credit”. There is no check point in the system. As an auditor, he must find that type of Wrong credit manually and arrive at the Correct NPA.
9. “Window Dressing”: The branch to have CASA deposit and Loan disbursement has adopted the method of transferring the amount from

Loan account to CA/SB account on a day before the Quarter ending day and the reversal of the entry from CA/SB to loan account is done on the next day of commencement of Quarter. This type of “Window Dressing” is easily possible in the system. In most of the branches there is “no” vouchers available and the Concurrent Auditor must verify those types of Entries.

10. Having Two Customer Identification Folio (CIF) in the Branch System will create lot of confusion in the form of “Group” sanction limit, NPA identification etc. As an Auditor, he must find the Number of CIF allotted to a particular account.
11. In operative Accounts must be verified by the Auditor, as there are lot of scope for misutilization of funds including Frauds. Unless and until proper checking and understanding of the Bank Software in the Banking system, it is very difficult to identify the same. The auditor must be fully equipped with the System operation and Full knowledge of the Banking software.

Chapter 3

Revenue Audit

3.1 Revenue audit is the audit of items governing income and expenditure of banks. Basically, this type of audit is conducted with a view to verify the accuracy and relevance of expenditure incurred and income earned by the banks according to applicable latest circular and notification. Auditor is only required to concentrate on the areas which affect revenue items of the bank.

3.2 Normal procedure to conduct the revenue audit is as under:

- Before commencing the revenue audit, the auditors are required to collect the list of auto levy (system levy) charges and manual levy of charges.
- Study the relevant circulars pertaining to charges given by the bank. Go through the format of audit report and annexure attached to the audit report.
- Prepare a separate file for audit and don't forget to carry audit engagement letter given by the appointing authority.
- Prepare the audit programme for all major areas to be covered.
- Auditors are advised to keep in mind the period of audit to set up schedule for audit, to ensure adequate and appropriate coverage and timely completion.
- Go through the previous revenue audit reports and concurrent audit reports of branch to get the overview of possible nature of leakage.
- Obtain some basic view about branch's banking software to facilitate easy viewing of customer ledger.
- Ask the branch to make available Advances Sanction Register for Audit Period.

With a view to obtain knowledge of accounts, an appropriate sample should be selected of following accounts:

- Cash Credit Accounts.

- Top Saving Account.
- Top Current Accounts.
- Top Term Deposit Accounts.
- Overdue advances in audit period.
- Premature Fixed Deposit Receipts (FDRs).
- List of NPA Accounts of branch and recoveries made during the period to be, appropriately, adjusted against interest/ instalment.

Income of Bank

List of areas to be covered for Income head and procedure for its audit are as under:

Interest Earned on Advances:

Under CBS rate of interests are being applied based on the advance products. Correct selection of advance product code is very important to apply appropriate rate of interest. Auditors are advised to check whether the advance master is created under the appropriate products. For example, ROI for housing loan product is different from mortgage loan. If housing loan is opened under mortgage loan product, ROI applicable for mortgage loan will be applied by the CBS system. The concurrent auditor should verify the rate of interest as per the sanction letter and it should be verified in the loan master.

Rate of interest has two parts namely:

Basic rate and Interest premium.

A Basic Rate

BPLR: Prime rate of interest is an interest charged by commercial banks to their most creditworthy customers. Thus, the bank would charge the lowest interest rate to the customers who had a good credit profile.

MCLR: Marginal Cost of Funds based Lending Rate (MCLR) is the minimum lending rate below which a bank is not permitted to lend. MCLR replaced the earlier base rate system to determine the lending rates for commercial banks. RBI implemented MCLR on 1 April 2016 to determine rates of interests for loans.

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EBLR: EBLR stands for External Benchmarks Lending Rate. According to the RBI's 5th bi-monthly Monetary Policy Statement (2018-19), floating interest rates for retail loans and micro and small businesses will be linked to EBLR. RBI also announced that further consultations would be held with stakeholders to develop an effective mechanism for transmitting rates.

B Interest Premium

Over and above the basic rate, financial institutions shall add interest premium rate decided based on the security cover, Sector risks, Borrower's financial risks and CIBIL scoring.

Auditors are advised to check whether the basic rate is correctly configured in the CBS and further interest premium is captured as input to arrive correct final rate of interest to be applied for the loan.

While verifying correctness of the ROI, following factors are to be considered:

- Check whether interest has been charged in accordance with applicable circulars of the bank.
- Check interest calculation on selective basis.
- Check whether interest has been charged as per ad hoc/ special sanction letter.
- Check that revised interest rates are properly applied in system from relevant date of applicability.
- Penal charges on overdue instalments and on late submission of Stock Statement/ Quarterly Monitoring Data (QMD). Generally, penal charges are to be charged 1% subject to maximum of 2%. Such panel interest is charged in following circumstances:
 - Instalment is overdue.
 - Amount exceeds the drawing power.
 - Delay in submission of stock statement.
 - Delay in submission of Quarterly Monitoring Data (QMD)/ Financial Statements.
 - Delay in renewal of working capital limits.

- Non-compliance of terms and conditions stipulated in the sanction letter.

CIBIL Charges

Check whether CIBIL charges are properly debited as per circular of charges. CIBIL charges are to be recovered for Borrower, co-Borrowers and guarantors also.

Processing fees

Processing fees is to be recovered on advances, as per sanction during audit period, wherever applicable as per circulars of charges, such as. Term loans, viz., housing loans, personal loans, vehicle loans, Cash Credits and overdrafts, Bank Guarantee/Letter of Credit/ Buyer's Credit Other Demand Loans. The auditor must verify that all processing charges levied by the bank are collected separately from the borrower's own resources and are not netted off against the sanctioned loan amount or deducted from the loan disbursement.

Cash Credit Renewal Charges

Cash Credit Limit should be renewed every year as per the terms and conditions of the bank. Verify the renewal register whether every cash credit account has been debited by cash credit renewal charges/ extension charges.

BG Commission Charges

BG commission charges shall be collected as per the service charges circular for the period of BG as well as claim period if any specified in the BG.

Inspection Charges

Verify that the charges are properly debited in borrower's ledger as per circular of charges.

Documentation Charges

Documentation charges should be debited in each sanction during the audit period as per the circular of charges.

Minimum Balance Charges

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These charges are, generally, debited on saving accounts/ current accounts and debited by data centre in case of CBS branches.

Verify some account on random basis that these charges are properly debited in accounts as per applicable circulars if account balance falls below minimum.

Ledger Folio Charges

These charges are to be charged to current accounts and cash credit accounts on basis of per ledger folio.

Generally, these charges are debited by data centre in case of CBS Branches, so selective accounts should be checked to determine whether charges are debited as per circulars.

Cash Recovery Against NPA Accounts

Confirm that all outstanding charges, interest outstanding are adjusted against such recoveries, then only principal amount of loan is adjusted.

Locker rent Charges

Generally, locker rent register is maintained by the bank and applicable charges are debited to saving account of customer. Auditors must check out whether charges as per circular have been debited to customer or not.

DD commission, IBC/ OBC commission, cheque book charges, stop payment charges

Obtain Pay order, DD register, IBC/OBC register from the branch and verify on selective basis that charges are properly debited to customer's account.

Obtain cheque book register and verify that series of cheque books are properly entered in register. When cheque book is issued to customer check series fed into the system so that cheque book charges are debited to customer's ledger.

Stop payment charges are debited on basis of per instrument basis (no of instrument* rate per instrument).

Income From Investment

Verify whether any investments have been made by the branch.

Obtain investment register from branch and verify whether interest and dividend are timely collected and accounted by the bank as per applicable rates.

Commitment charges for the facilities not utilised/ short utilised

Many banks have started levying penal charges for short utilisation/ non-utilisation of cash credit/ term loan facility. Revenue auditors are required to check the bank policy on levying such charges and accordingly, verify the same with the statement of accounts.

Debit/ Credit Card related charges:

These charges are to be charged to the customer for the following:

1. Debit/credit card annual fees.
2. Card replacement charges.
3. PIN generation charges.
4. International transaction charges.
5. Cash advance charges.
6. Overlimit charges.

The auditor needs to verify whether charges as per the bank circular have been debited to customer or not.

Solvency Certificate Charges

These are charges collected by the bank for issuing a solvency certificate, usually required by customers for tender submissions, court affidavits, government requirements, etc.

Verify proper debit of charges to customer's account as per Schedule of Charges approved by the bank. Ensure the solvency certificate is issued only after proper due diligence, such as: Analysis of customer's financials.

Cash Deposition Charges

Banks levy charges for depositing cash over free limits, especially in current accounts, non-home branches, or third-party cash deposits.

Check if charges are levied as per policy for:

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1. Excess cash deposit over limits.
2. Deposits at non-base branches.
3. Third-party depositors.

Reconcile income with CBS reports to verify no undercharging.

Debits to Income Account Charges

These are entries where the branch debits the bank's own income account (usually GL accounts) — could be due to:

1. Reversals of wrongly collected charges
2. Waivers
3. Incentives or adjustments

Scrutinize all debits to income heads, especially manual ones. Verify if there is authorization for reversal — check for:

Approval from branch head / Zonal Office

Check for recurrence patterns — are reversals frequent for certain customers?

Demat Charges:

Auditor should verify the demat charges as specified by the bank as communicated by the demat department.

Pending Demat charges - To check whether follow up is being done to recover lien noted in system for pending Demat charges.

Expenses of Bank

Following are the major heads to be verified by the auditor related to expenses of bank:

Interest paid on Deposit Accounts

Generally, banks give credit of interest to customer's account on half yearly/ quarterly basis by giving command of Interest Credit in case of CBS Operation. Auditor must check on selective basis whether interest has been credited on due time and at appropriate rate as per the applicable circulars.

Interest on Term Deposits

Whether the rates fed in the system are as per policy of the bank.

In case of premature repayment of deposit, applicable penalty and reduced rate of interest has been charged.

If a term deposit matures and proceeds are unpaid, the amount left unclaimed with the bank shall attract rate of interest as applicable to saving account.

Interest on overdue Domestic Deposits

If a Term Deposit (TD) maturity and proceeds are unpaid, the amount left unclaimed with the bank shall be a rate of interest as applicable to savings account or the contracted rate of interest on the matured TD, whichever is lower.

General Branch Expenses

General branch expenses are as per delegated power on respective accounts.

Legal/ Valuation Charges

Legal/ valuation charges on non-performing accounts are as per schedule of charges.

Chapter 4

Vertical Based Concurrent Audit

5.1 The new concept of converging the banking operations into different verticals is practiced by many banks with a focus on specific industry segments or customer groups with specialized products and services. This contrasts with the traditional approach of horizontally focused banks that offer a wide range of products to general customers. Vertical banking allows banks to gain a deeper understanding of niche needs, build stronger relationships, achieve high level specialization and potentially command a premium for their services. The banks by and large are consolidating the loan processing and disbursement of various branches under one cluster. These clusters are designed as different types of offices as Regional Centers or Hubs as per bank's discretion.

Some benefits / Features of cluster approach:

- Specialization in Services.
- Increased Efficiency.
- Better Customer Understanding.
- Access to New Markets.
- Competitive Advantage.
- Digital Transformation.

5.2 Clusters / Loan Products: The cluster will be only focusing on loan processing, sanction and disbursement of specific product verticals allotted to the cluster. The branches will be acting as collecting centers of loan applications and necessary papers / documents. The borrower applications are pushed to the cluster for processing, sanction, documentation, disbursement and monitoring.

However, with the advent of Information Technology & Digitization, most of the banks have been handling the process of submission of applications and all the documents required along with the same through digital process. Websites of the banks can be visited for submission of applications and all necessary documents. Tracking of the status of the loan application can also

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be made. Banks have also developed mobile applications for some of these services. Concurrent audit is now conducted at the cluster assigned with verticals of loan products. Various loan products are categorized and grouped under one cluster. Hub offices of major banks are known as follows:

1. RASMEC, RACPC etc. in State Bank of India.
2. Retail Loan Point (RLP), MSME Loan Point (MLP) in Union Bank of India.
3. Retail Asset Hub in Canara Bank.
4. Centralized Loan Processing Center (CLPC) in Punjab Nation Bank.
5. CMOG in South Indian Bank.

The loan products handled in Verticals are as under:

- Personal Loans
- Vehicle / Automobile Loans
- Educational Loans
- Home / Housing Loans
- MSME Loans
- Agriculture Loans
- Start-ups
- Financial Inclusion

Concurrent Audit Methodology: Majority of the concurrent audit in these cluster are system driven and structured by a process of straight through mechanism in the audit module of the bank. The Concurrent Auditor is expected to conduct the audit and report his audit observations online in the system platform as per the structured checklist provided by the bank in the audit module. The salient features of the concurrent audit methodology are as under: "Concurrent Auditor should understand the nature of the Vertical / Cluster, underlying number of branches coming under the cluster and loan product/s handled in the cluster. The scheme of the Bank for the loan products should be thoroughly gone through from the brochures & other materials of the Bank. Auditors should get acquainted with various legal requirements and provisions applicable to the loan products. The Concurrent Auditor should evaluate the scope of work given by the Bank.

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- Concurrent Auditor should get acquainted with the Audit Module i.e. the software used by the Bank for informing audit observations to the Bank and for incorporating the audit report. The entire process is now system driven in most of the banks and the audit report preparation must be completed in the branch premises itself.
- Concurrent Auditor should conduct verification of documents of loan sanctioned at the cluster with specific reference to loan application, various KYC documents, other documents submitted along with application, loan appraisal note prepared by the Bank and sanction, security documents obtained from the borrower, insurance, compliance of CIBIL, CRIF, CRILIC, CERSAI, etc. in line with the requirement of checklist provided in the system.
- The observations should be punched into the system format and would be pushed to the compliance officer within the cluster for rectification of the discrepancies or deficiency.
- The compliance officer will revert with the rectification to the concurrent auditor who will again verify the compliance as in order and withdraw the observation in the system.
- In the case of observations which require more time for compliance, considering the practical and legal delay, it will be marked in the system as deferred for future compliance with time specifications.

E.g.:

- Obtaining the lien marking on RC books in case of vehicle loans.
- Getting the registration of Sales Deed and completion certificate in case Housing Loans granted for purchasing flats.

The compliance of such observations will be further monitored and followed by the Concurrent Auditor till such a time it is completely resolved:

- The number of observations initially made, the number of observations rectified and the number of observations still pending for compliance will be reported by the system through auto populated platform.
- The controlling officers will monitor and follow up the compliance and closing out of observations with the branch on an ongoing basis.

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- The summary of the accounts verified, observations made, critical points etc. will be reported to the Bank monthly or as specified by the Bank in the letter of appointment.
- Apart from the verification of loans, the scope of concurrent audit also would include verification of revenue leakages, legal compliance, disbursement voucher verification, housekeeping etc. For every function of addons to the concurrent audit, separate platforms in the audit module are designed by the bank. The auditor is expected to report every aspect through the system and submit the report online to the controlling authorities.

General Aspects of Loans and Advances Verification

- Application form.
- KYC/ Identity Proof Documents (Aadhaar, PAN, Voter ID, Passport).
- Address & age proof documents.
- To ensure that KYC documents have been verified online from the respective website.
- Pre-sanction inspection to the registered address of residence/ workplace/ business place of borrower is conducted by the Bank's officials and properly documented.
- In respect of Salaried Employees.
- Latest Salary Slip/ Certificate.
- Bank account statement for last 6 months, duly certified.
- Employers' undertaking for deduction of salary at source is accepted and confirmed.
- Verification of employer Company profile has been carried out and copy held on record.
- Income Tax Returns.
- Copies of IT returns for the last 3 years.
- To ensure that IT returns for past years were not filed in a single year.
- Business/ Professionals.

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- Financial statements (duly audited as required) for the past 3 years.
- Bank account statement for last 6 months, duly certified.
- Income proofs, IT returns, TIN/ GST registration number, Status of Income Tax Return, Tax Paid Challan etc. have been verified by the branch from the concerned website.
- All Liabilities are considered to arrive at the Net worth.
- The CIBIL/ CRIF report on borrowers generated from the respective platform is kept on record.
- The Central Fraud Registry website has been verified, if required, as per the bank's guidelines.
- Lien has been marked on Term Deposits held as security in the system.
- Proper Updating of Master Data in CBS.
- KYC particulars.
- Contact Details of borrower(s) such as Mobile Number, e-Mail IDs, address etc.,
- Loan scheme code.
- Amount sanctioned.
- Rate of Interest.
- Repayment schedule.
- Interest payment date.
- Moratorium period.
- Amount of Instalment/ EMI.

The critical verification points which require concurrent auditors' acumen and wisdom in each product category are briefly narrated below. The Online check list provided by the bank, apart from others would contain the following important Questions to be verified and answered through the system check list by the concurrent auditors:

- 1) Car Loans
- 2) Educational Loans
- 3) Loan Against Property

4) Cash Credit/ Overdraft

Car Loan

Aspects of Verification

Vehicle Automobile Loans

For new vehicle:

- Quotation from the Dealer of the vehicle. The bank has ensured appropriateness of the price of the vehicle.
- If the loan is for purchase of a certified pre-owned car, the car is not more than prescribed number of years old.
- Receipt for the margin money, payment is obtained, or account statement is kept with records for having verified payment of margin money by cheque.
- Disbursement is made by transfer if dealer has an account with the Bank and through NEFT/ RTGS, where dealer is not having account with the lending Bank.
- Copy of RC book with lien marked in favour of bank for the loan taken should be ensured.
- Signed RTO forms as per respective motor vehicles act are kept on record.
- Vehicle registration details have been verified from the website vahan.nic.in" within 30 days from the date of disbursement and screen shot from site duly verified has been kept with documents.
- Copy of Registration Certificate with Bank's charge noted therein/Extract from vahan.nic.in extract from R.T.O. is on record.
- Extension of Charge on existing primary and/or collateral security is created for high value loans as per extant guidelines.
- To confirm, insurance policy with Bank's hypothecation charge is taken on record.

In case of loan for purchase of commercial vehicle to check following documents are taken on record:

- a) Tourist Permit (PCoT).

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- b) Commercial Driving License (Driver badge).
- c) Police verification certificate.

In case of loan for purchase of commercial vehicle to check condition regarding, Board of Hypothecation with bank with bold letters to be printed to the back side of vehicle.

To check in case of loan sanctioned for purchase of Second-Hand Vehicle:

- Whether valuation report from panel valuer is obtained.
- Whether age of second-hand vehicle is considered.

Educational Loan

Aspects of Verification

- Academic record/ performance of the applicant has been scrutinised from mark sheets/ certificates.
- The standing and reputation of the education institution is verified with accredited list of Institutions of the bank.
- Admission letter/ offer letter from the educational institution.
- Statement of cost of studies & living expenses and sources thereof (own sources & loans).

Loan Against Property

1. In case of salaried applicants, verification of employer Company profile has been carried out and copy held on record.
2. Copy of IT return for 3 years with latest salary slip and bank account statement for 6 months obtained in respect of all borrowers/ Guarantors, whose income is reckoned for arriving the repayment capacity.
3. Property offered is un-encumbered/ non- Agricultural and is SARFAESI compliant.
4. Residential house or Flat in the name of the borrower/ guarantor in Metro/ urban areas should be as per local building rules.
5. Verify the approval of flat or building projects as per RERA of the local laws.

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6. Property offered, if rented out, the respective lease agreement and its covenants to be verified.
7. Valuation certificate is obtained from the panel valuer. Property values are ascertained from general online portals available.
8. Property inspection is documented and signed by the bank officials.
9. Photograph of the property is enclosed along with the photo of the Official who inspected the site.
10. Satisfaction of valuation by the branch official is documented and signed by the bank officials.
11. CERSAI site is verified before sanction of the loan and kept with the loan document with CERSAI registration papers.
12. Assets & Liabilities statement obtained from the borrower(s)/ Guarantor(s) are properly scrutinised for commitments of other loan repayments.
13. Post sanction inspection report is kept on record.
14. Equitable Mortgage is properly created in respect of all properties mentioned in the sanction. All the documents mentioned in the legal scrutiny report have been obtained.
15. Recital of Equitable mortgage creation has been recorded in title deeds register/ Memorandum of Deposit of title deeds (Wherever applicable) containing the correct description of the title deeds as in SRO.
16. Post registration Encumbrance Certificate for the broken period has been obtained and held on record.
17. After total repayment of loan dues, the bank shall release the property related documents and hand it over to the borrower.

Points to be Considered for Verification In case of Creation of Mortgage

1. Accurate and full description of properties along with ownership, Date of valuation, SARFAESI compliance, Date and report of property visit by branch officials, is recorded in the proposal.
2. Valuation Report(s) (two valuation reports from different empanelled valuers in case of all loans of above prescribed limit) have been

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obtained from empanelled valuer for all the properties, on the prescribed formats of the bank.

3. In case of variation of 20% or more in the valuation proposed by the valuer and the Govt. Guideline value, then the justification for variation is given. Details of last two transactions if available in the area, have been incorporated in the Valuation Report. Property values reported in leading newspapers as well as public online property portals wherever available are referred to and quoted.
4. Photo of the Inspecting Official at the site taken as an integral part of inspection and kept along with the security documents with date and time.
5. Value of Primary securities as per the latest Valuation Reports has been incorporated in master data.
6. Value of Collateral securities as per the latest Valuation Reports has been incorporated in master data.
7. Banks laid down procedures as under have been followed while creating Equitable Mortgage based on certified copies of the Title deeds where Original Title deeds are lost/ destroyed etc.
 - Sanction from higher authority is obtained.
 - FIR or Diary Report about loss of document is filed with detailed facts.
 - Borrower/ Guarantor has given notice of public advertisement in one leading National and in one Regional News Paper clearly stating the intention to create charge viz Mortgage or otherwise based on certified copy of Title deed that it has been lost by giving with full detail of relevant property (s).
 - Obtaining stamped affidavit-cum-declaration from borrower/ guarantor containing declaration that title deed in original is lost.
 - Independent verification/ identification of property and mortgagor to be ensured by branches.
8. If Ownership of Property is derived to the borrower as per gift deed, clearance from the appropriate authority is obtained.

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9. Wherever Agreement to Mortgage is obtained, the title deeds relating to the properties described in the schedule thereto are handed over to the Bank along with non-encumbrance certificates.
10. All original title deeds/ Linked title deeds as stipulated in the legal scrutiny report are held on record.
11. In case of loan against corporate property, Search Report from Registrar of Companies (ROC) to be obtained.
12. Encumbrance Certificate for a period not less than 13 years/ 33 years as per bank policy guidelines.
13. Mother title documents have been adequately furnished in the legal opinion based on parent/ subsequent title deeds.
14. Demarcation of the land has been commented with Boundaries/ extent covered etc.
15. Applicability of SARFAESI enforcement, special category of Agricultural properties and properties covered under ECO Fragile Land, Coastal Zone etc to be identified.
16. Certified copies of title deeds issued by SRO are enclosed as per bank guidelines.
17. Mortgage created through the power of attorney, if any, is executed in presence of bank officials at foreign offices or Indian embassy in case of NRI customers, not able to visit India.

Cash Credit/ Overdraft

1. The sanction Letter of the competent authority should be kept on record and the auditor should verify the compliance of conditions/terms of sanctions and disbursement.
2. The deed of Constitution as Partnership Deed, Articles of Association, Memorandum of Association, Trust Deed, Bye laws etc. as the case may be, is kept on record.
3. Board/ Partners Resolution etc. for obtaining loan and also acknowledging the terms and conditions of sanction to be obtained on record.
4. The validity/ amendment/ legal covenants and restrictive clauses in the constitution deed should be critically examined.

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5. KYC and all address proof of all parties to the loan should be obtained and approved by the centralised KYC Hub.
6. CIBIL/ CRIF/ CRILIC are properly verified and the score vet by the bankers.
7. The documents substantiating the repayment capacity and financial standing of the borrower such as Balance Sheet, Profit and Loss account, Cash Flow, Income Tax records, GST Return Copies, Other statutory returns should be examined and commented for any deficiencies.
8. Documented reports of Presanction and Post Sanction inspection is kept on record.
9. The Details of primary security, its margin and the conditions attached to the calculation of Drawing Power against the primary Security should be verified.
10. The Periodical filing stock statements, Debtors statement should be verified and factored in master for Drawing Power Up dation.
11. Ensure obtention of Certificate of Chartered Accountants prescribed for Debtors ageing and Debtors balances should be verified.
12. The conduct of stock audit and the stock audit report should be verified and any discrepancies as per stock audit report addressed by the bank.
13. The Hypothecation Agreement and the relevant connected documents for charge on primary security to be ensured.
14. The Creation of Charge, Modification of charge etc. is vet with the search report obtained from the Registrar of Companies in case of company borrowers.
15. Creation of Equitable Mortgage of properties held as collateral should be verified. (**Refer to all points covered above**)
16. Check out the Insurance of Primary Security and Collateral Security covering all possible RISK is adequate is not expired.
17. Waiver of conditions attached to the loan product as per sanction terms should be verified with the sanction document.

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18. Comment on the turnover in the account and any aberration between the turnover reported as per financial statements and magnitude of transactions put through bank account.

The entire process of cluster based concurrent audit is system driven and the auditors log and log in details would be monitored at the controlling office. The follow up and closing out of compliance is more emphasised by banks in this system to ensure concurrent corrections and regularisations. The module will be of a questionnaire / check list type to be filled in by the auditors in the system online.

Gold Loans

- I. The individual borrower-wise and sectoral limits laid down by the Bank for gold loans have been adhered to in case of each loan a/c.
- II. Repayment capacity of the borrower is properly assessed in case of large loans (above a threshold).
- III. Streedhan Certificate is obtained in case of jewellery & ornaments of ladies pledged.
- IV. To ensure that assessment of purity of gold and weight of gold is done by the Saraf (Assayer) who is duly empanelled with the Bank. Validity of bank's agreement with Saraf to be ascertained (copy of agreement is usually held by branches along with specimen signatures of Saraf).
- V. Gold ornaments are properly sealed and kept in vaults of the branch.
- VI. Valuation of gold is done by the Branch at appropriate intervals of loan to value ratio is maintained as per the policy of the Bank. Valuation should be done in case of reduction in the prices of the gold to ensure this aspect.
- VII. Gold packets should be verified to ensure that security is held by the Bank for each gold loan. Frequency and test check should be decided by the Concurrent Auditor. Concurrent Auditor shall ensure the due process is followed with respect to verification of purity and weight of the gold by Assayer.
- VIII. Concurrent Auditor shall confirm the End use of funds is verified by bank for all loans (above a threshold limit specified by the Bank) and proper evidence is kept on record. For advances against gold coins the end use of funds is done for approved and non-speculative purposes.

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- IX. In case of loans against gold for agriculture purpose & classified as agriculture loan, the Bank has ensured that the borrower / spouse is agriculturist. Copies of land records (7/12 extract) have been obtained, and the bank has ensured that end use of the loan is made for agriculture purpose only.
- X. Evergreening of loans is not done, in case the gold loan a/c is turning into NPA, by sanctioning another gold loan to the same borrower / spouse, either on the same day/ next day of the closure of the existing loan a/c. Proper care is taken in case of renewal of gold loans and top up loans disbursed.
- XI. Instalment and interest on loan is recovered as specified in the sanction (except where bullet repayment is sanctioned) Overdue, if any, are properly classified and reported. Follow-up should be made by the Branch for recovery thereof.
- XII. In case of auction of gold ornaments, procedure laid down by the Bank is properly followed and due care is taken by the Branch.
- XIII. Concurrent Auditor should ensure that any other conditions as specified in the credit policy/ circular issued by the Bank for loans against gold have been complied by the Branch.

Agriculture Loans

Concurrent Auditor should get acquainted with various special features of agricultural advances, such as:

- (i) Categories of farmers (marginal, small, medium, large) Crop cycles (Kharif, Rabbi, other).
- (ii) Types of activities covered under agriculture & excluded from agriculture, allied activities.
- (iii) Scale of Finance for various crops sanctioned by State Level Bankers' Committee. Scale will be different state-wise.
- (iv) Types of Loans sanctioned to farmers including Crop Loans and Kisan Credit Card.
- (v) IRAC norms for agriculture loans based on crop seasons. Natural calamities occurred and its' impact on IRAC classification.

Vertical Based Concurrent Audit

- (vi) Methodology for charging of interest on agriculture loans, which is linked to crop seasons.
- (vii) Interest Subvention schemes for agriculture loans.
- (viii) Loan waiver schemes declared by respective state govt., if any and its' impact of loans Auditor needs to ensure that advances for purposes other than agriculture are not classified under this category.

Verification to be conducted for Agriculture Loans

- I. Application form duly filled along with copies of 7/12 extracts (land records).
- II. Sanction as per scale of finance applicable to the land under cultivation & crop being cultivated.
- III. Loan extended only after obtaining 'No dues/ No objection Certificate' from the existing credit agencies.
- IV. Security - Standing crops, Agricultural machinery & implements secured by hypothecation (primary security), Agricultural land secured by a mortgage charge (secondary security), To confirm legal enforceability of security.
- V. Disbursement - Disbursement in various 'stages' based on the requirements of farming activity.
- VI. Expenditure incurred by farmers from own sources or from non-institutional lenders & subsequently reimbursed by banks.
- VII. Verify the facts from the documents/ evidence available on record- Documents evidencing the utilisation of loans for agricultural activities. Even if gold loan is sanctioned for agriculture purpose, utilization will be required to be monitored.
- VIII. Recovery to ensure that recovery in loan a/cs is coming thorough sale of crops and not any other sources. Nature and timing of recovery needs to be verified. Monitoring.
- IX. To ensure that adequate monitoring is done by the Bank during appraisal, disbursement and post disbursement phase by obtaining appropriate documents and by visit to the farms.

Reverse Mortgage

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1. Reverse mortgages are powerful tools that help eligible homeowners obtain a tax-free cash flow.
2. A reverse mortgage is a government sponsored and insured loan that requires no payments during the period, borrowers live in their home.
3. Reverse mortgages enable eligible homeowners to access the money they have built up as equity in their homes. Conceptually, a reverse mortgage seeks to monetize the house as an asset and specifically the owner's equity in the house.
4. Senior Citizen who has cross 60 years of age are eligible to obtain the Reverse Mortgage Loan.
5. The Reverse Mortgage Loan must be repaid only after the Lifetime of the borrower. In case the Borrower wants to repay the loan during the lifetime it can be repaid.
6. This loan is sanctioned only to the Self Acquired property with Self Occupation.

Appendix I

Engagement Letter for Concurrent Audit

Date: xxxx

Board of Directors / Audit Committee

xxxx Bank

xxxx

xxxx

Dear Sirs,

Sub.: Engagement Letter for Concurrent Audit

We refer to your letter no. xxxx dated xxxx received from xxxx (Name of the relevant authority) of xxxx Bank, informing about (re)appointment of xxxx, Chartered Accountants (hereinafter referred to as the Firm or the Concurrent Auditors) to conduct Concurrent Audit of following branches / offices of xxxx Bank (hereinafter referred to as the Bank) for the period from xxxx to xxxx.

Branches / Offices allotted for Concurrent Audit:

- i. Xxxx (code xx) ii. Xxxx (code xx) iii. Xxxx (code xx)

We are pleased to confirm our acceptance and understanding of this engagement by means of this letter.

The purpose of this letter is to set out the basis on which we act to conduct the Concurrent Audit of the aforesaid branches / offices of the Bank, our understanding of the Objectives and Scope of this engagement and respective areas of responsibility of the Bank and Concurrent Auditors.

Objectives

Concurrent Audit aims at shortening the interval between a transaction and its independent examination. It is integral to the establishment of sound internal accounting functions and effective controls and is regarded as part of a bank's early warning system to ensure timely detection of serious errors and irregularities, which also helps in averting fraudulent transactions and preventive vigilance in banks

Scope of the Engagement

The Scope of the Concurrent Audit engagement shall be as per the “scope / areas of coverage” as specified in the annexure to the letter of appointment dated xxxx from the Bank, which is enclosed to this Engagement Letter. The scope of the audit as specified above may be revised by the Bank from time to time, by inclusion of additional items, and will be communicated by the Bank to the Concurrent Auditors, acceptance for which will be communicated by the Concurrent Auditors.

The Concurrent Audit will also ensure coverage as per prevailing RBI guidelines conveyed vide circular no. DBS.CO.ARS.No.BC.01/08.91.021/2019-20 dated 18-09-2019.

The above scope of audit is to be covered as under as specified by the Bank in the letter of appointment dated xxxx:

- (a) Daily Activity
- (b) Weekly Activity
- (c) Fortnightly Activity and
- (d) Monthly Activity

Any additional assignment, other than in the nature of concurrent audit, given by the Bank will be considered and accepted by the Concurrent Auditors, provided that such assignments are within the framework of the code of Ethics and other regulations of the Institute of Chartered Accountants of India.

Audit Team & Attendance

The Firm shall depute audit team consisting of xxxx, xxxx, as specified in the letter of appointment dated xxxx. The audit team will be led by xxxx.

The audit team shall visit the branches / offices of the Bank, for xx days during the week / month, as specified in the aforesaid letter.

Compliance with Standards on Internal Audit

We shall conduct the Concurrent Audit under various Standards on Internal Audit issued by the Institute of Chartered Accountants of India (ICAI) from time to time.

Concurrent Audit Report

The Firm shall prepare the Concurrent Audit Report on monthly / quarterly basis, through the web-based audit report software introduced by the Bank and submit the concurrent audit report (soft copy) through email to the branch under audit and to the controlling offices, as specified in the letter of appointment dated xxxx. Apart from the above report, any serious irregularities or fraud prone transactions observed the Concurrent Auditors shall be reported by way of a special report, which shall be submitted immediately by the Auditors to the authorities specified by the Bank in the letter of appointment dated xxxx.

The Firm shall follow the time norms prescribed by the Bank for completion of the audit and submission of the audit report.

Communication with those charged with Governance

We presume that the scope and timing of the work concurrent audit work has been communicated by the Bank to “Those Charged with Governance” (TCWG) and as such separate communication from us is not required. Also, our concurrent audit reports will be sent to various authorities of the Bank, as specified in the letter of appointment and not directly to TCWG. We understand that significant audit findings communicated by us in our concurrent audit reports will be informed by the Bank to TCWG.

Authority of Concurrent Auditors

The Concurrent Auditors shall have requisite authority including access to the CBS System, other Application Softwares & other computerised systems, books, records, vouchers, documents, information etc., wherever kept by the Bank, which are required for the purpose of conducting the concurrent audit engagement. Concurrent Auditors shall have access to reports submitted by other agencies such as Statutory Audit / Long Form Audit Report, Internal / Risk Based Internal Audit, Revenue Audit, Stock Audit, Legal Audit etc.

The Concurrent Auditors shall have authority to call for information and explanations from the concerned officials of the Branch and also the Controlling Offices, as required.

Responsibilities of the Concurrent Auditors

Concurrent Auditors shall complete the Concurrent Audit Assignment as per the guidelines / instructions given by the Bank and submit the Audit Report, as per the timelines agreed with the Bank.

However, Concurrent Auditors shall not be responsible for delay in completion of the assignment and submission of the reports due to the causes beyond their reasonable control.

Observations on statutory regulations, included in the report, shall not purport to be an opinion, expert or otherwise on these matters. They merely represent our understanding of the facts and possible interpretations of law. The Bank is advised to take expert opinion in these cases, before initiating any action.

As early detection of errors, irregularities and fraudulent transactions is the objective of this Concurrent Audit engagement, Concurrent Audit shall help in averting fraudulent transactions. As such, serious irregularities and suspected fraudulent transactions observed, if any, during the course of conducting concurrent audit engagement shall be communicated immediately to the Bank for further action.

Responsibilities of the Bank

The Bank is responsible for designing proper internal control system consisting of controls in CBS system as well as manual internal controls and also maintaining and ensuring operating effectiveness of the system of internal controls in its' operations & accounts. The Bank is also responsible for compliance of laws and regulations as applicable to its' business activities and communicating lapses, if any, to the regulatory authorities.

The Bank shall provide necessary access to the CBS System, other Application Softwares & other computerised systems, books, records, vouchers, documents, information etc., wherever kept by the Bank, which are required for the purpose of conducting the concurrent audit engagement.

The concerned officials of the Branch and also the Controlling Offices shall provide necessary information and explanations to the Concurrent Auditors, as required.

The Bank shall also allow Concurrent Auditors to extract various reports from the CBS System and other application softwares / computerised systems of

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the Bank in electronic form, necessary for the purpose of conducting Concurrent Audit and allow the same to be transferred to the computers / laptops of the Concurrent Auditors. In case of bulk reports, the Bank shall extract the same from CBS system and provide the same in electronic form to the Concurrent Auditors on their laptops / computers.

Concerned Officials of the Bank shall, within a reasonable time, provide replies to queries communicated by the Concurrent Auditors, so as to facilitate to complete the audit within the prescribed time frame.

The officials of the Branch shall take steps to rectify on the spot minor irregularities pointed out by Concurrent Auditors. The Branch should ensure rectification of other deficiencies without any loss of time so as to achieve the purpose of Concurrent Audit. The Branch shall submit the compliance report / action taken report based on the audit report furnished by the Concurrent Auditors.

Review of Performance of Concurrent Audit

We understand that the Bank shall conduct review of effectiveness and performance of the Concurrent Audit conducted by our Firm, during the course of tenure of the engagement and take necessary steps, as per the Bank's policy, if the performance is not found satisfactory.

Confidentiality

Confidentiality of Working Papers

The working papers and other electronic documents prepared in conjunction with the Concurrent Audit are the sole property of Concurrent Auditors, constitute confidential information and will be retained by us in accordance with our policies and procedures. However, we hereby acknowledge that the details or data received from the Bank for preparation of these working papers are confidential information of the Bank and will not be disclosed by us to any third party, except for the purpose of peer review / quality review as set out in this letter or when required by the regulators or under legislation, without the prior written consent from the Bank and with intimation to the Bank, if permitted by the Regulators.

Confidentiality of Concurrent Audit Report

The Concurrent Audit Report (including Executive Summary) shall be meant solely for the use by the Bank internally. The Concurrent Audit Report shall

not be distributed or circulated by the Bank or by the Concurrent Auditors to any party unless there is a statutory or a regulatory requirement to do so.

The Audit Report should not be used, quoted or referred to by anyone other than the Bank, except as stated above. Concurrent Auditors assume no responsibility towards any such users of the Report, other than the Bank.

Peer Review & Other Regulatory Reviews

In accordance with the Statement on Peer Review issued by the Institute of Chartered Accountants of India or as may be required or mandated by any other competent regulator, our services covered by this letter may be subject to a review to be conducted by an independent reviewer who can inspect, examine or take abstract of our work papers including those provided by the Bank. Similarly review of our records and audit working papers may be conducted as per directions issued by any Regulatory Authority.

We undertake to provide the audit working papers for review by the Bank, when called for.

Neither party shall have any confidentiality obligations with respect to any information that is disclosed pursuant to applicable law, regulation, subpoena, other legal process or professional obligations, or in connection with the enforcement of the recipient's rights under this Agreement.

Force Majeure

Concurrent Auditors shall not be liable for any failure to perform the assignment within the stipulated time frame arising from causes beyond our control, including, but not limited to, pandemic, epidemic, fire, storm, flood, earthquake, explosion, accident, theft, terrorism, acts of public enemies, war, insurrection, sabotage, acts of God, or acts of any governmental authority or agency thereof.

Professional Fees

The professional fees for the assignment shall be Rs. xxx per month / quarter.

Goods & Services Tax (GST) thereon at the applicable rates (at present 18%) shall be charged extra, in addition to the above fees. The professional fees shall be subject to deduction of tax at source, at the applicable rates.

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Professional fees shall be payable on submission of the Concurrent Audit Report.

Updating UDIN

We also wish to inform that pursuant to the ICAI regulations, we are required to update certain relevant details of the branches / offices of the Bank audited by us, in the Unique Document Identification Number (UDIN) Portal of the ICAI for generating the UDIN reference number, which is required to be stated in the report issued by us to the Bank.

Agreement of Terms

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our aforementioned assignment/s including our respective responsibilities. Please also mark a copy of such acknowledgement to the concerned official/s of the respective branches / offices.

For xxxx

Chartered Accountants

Firm Registration No: xxxx

xxxx

Partner

Membership No. xxxx

Acknowledged on behalf of the Bank

For xxxx Bank

xxxx

Designation

Appendix II

CBS Commands

List of CBS Commands

Sr	Finacle 7 Menu	Finacle 10 Menu	Description
1	BRDEAF	BRDEAF	DORMANT ACCOUNT MAINTENANCE
2	BRPCINT	BRPCINT	Interest run on RPC Accounts (a/c wise)
3	BLRTI	BTPM	Bills Register Type Inquiry
4	DCRM	DCTPM	Documentary Credits Register Maintenance
5	AACM	HAACM	Accounts Access Code Maintenance
6	ABMR	HABMR	Report of Accounts Below Min Balance
7	ACCBAL	HACCBAL	Components of Account Balance Inquiry
8	ACDET	HACDET	Account Balance Details
9	ACI	HACI	Customer Accounts Inquiry
10	HACLHM	HACLHM	Account Limit History Maintenance
11	ACLI	HACLI	Account Ledger Inquiry
12	ACLPCA	HACLPCA	Customer Account Ledger Print
13	ACLPOA	HACLPOA	Office Account Ledgers Print
14	ACM	HACM	Customer Accounts Maintenance
15	ACMP	HACMP	Account Master Print

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16	BRACS	HACSP	Account Selection - BancsRemote
17	ACTI	HACTI	Account Turnover Inquiry
18	ACTODI	HACTODI	Account TOD Inquiry
19	HACTODM	HACTODM	Account TOD Maintenance
20	HAITINQ	HAITINQ	Account Interest Details Inquiry
21	BIACCR	HBIACCR	Interest Accrual For Bills
22	BINTRPT	HBINTRPT	Interest Report For Bills
23	DCQRY	HBKDCI	Query on Documentary Credits
24	BR	HBR	Balancing Report
25	BRBPR	HBRBPR	Balancing Report - Bills Purchased
26	BRCR	HBRCR	Balancing Report - Collection
27	BLRTM	HBRTM	Bills Register Type Maintenance
28	CACMMU	HCACMMU	Accounts Maintenance Menu
29	CAINTMU	HCAINTMU	Accounts/Bills Interest Menu
30	CBR	HCBR	Cash Balance Report
31	CIPPRPT	HCIPPRPT	Customer Interest Pref and Peg Report
32	CLCM	HCLCM	Charge Level Code Maintenance
33	CLL	HCLL	Collateral Lookup
34	CLSRPTS	HCLSRPTS	Collateral Status Reports
35	HCUDET	HCUDET	General details of Customer
36	CUIR	HCUIR	Customer Interest Report
37	CULAC	HCULAC	Customer Accounts List
38	DCLIABRG	HDCLIABRG	Documentary Credits Liability Register

39	DCREG	HDCREG	Documentary Credits Register Printing
40	DDIR	HDDIR	DD Issue Reports
41	DPGR	HDPGR	Deferred Payment Guarantee Register
42	EXCPRPT	HEXCPRPT	Exceptions Report
43	FBBR	HFBBR	Foreign Bills Balancing Register
44	FTI	HFTI	Financial Transactions Inquiry
45	GILR	HGILR	Guarantees Issued cum Liability Register
46	HINTTI	HINTTI	Interest Rate Details Inquiry
47	LAMP	HLAMP	Loan Account Master Print
48	HLAOPI	HLAOPI	Loans Overdue Position Inquiry
49	HLARA	HLARA	Loan Amendment and Rescheduling
50	HLARSH	HLARSH	Loans Repayment Schedule Report
51	HOAI	HOAI	OFFICE ACCOUNT INQUIRY
52	RPCRPT	HRPCRPT	Reports Of RPC Accounts
53	SII	HSII	Standing Instructions Inquiry
54	HTDSIP	HTDSIP	TDS Inquiry & Printing
55	BEHI	IBH	Bills Events History Inquiry
56	BI	IBL	Bills Inquiry
57	RINTINQ	IPCI	Interest Inquiry For RPC Accounts
58	NPAINQ	NPAINQ	NPA Status Inquiry Menu

Abbreviations

AAP	Annual Action Plan
ABBF	Advisory Board on Bank Frauds
ACRC	Agricultural Credit Review Committee
ACB	Audit Committee of Board of Directors
ACU	Asian Clearing Union
AD	Authorised Dealer
ADB	Asian Development Bank
ADF	Asian Development Fund
AFS	Audited Financial Statement
ATR	Action Taken Report
ALPM	Advanced Ledger Posting Machine
AMC	Asset Management Company
AOD	Acknowledgment of Debt
APEC	Asia Pacific Economic Cooperation
ASSOCHAM	Associated Chambers of Commerce and Industry
ATM	Automated Teller Machine
ADR	American Depository Receipt
ALM	Asset -Liability Management
ARC	Asset Reconstruction Company
ARDB	Agricultural Rural Development Banks
ARDC	Agricultural Refinance and Development Corporation
BIP	Bankers Indemnity Policy

BIFR	Board for Industrial and Financial Reconstruction
BIS	Bureau of Indian Standards
BOLT	Build-Own-Lease-Transfer
BoP	Balance of Payments
BRs	Bank Receipts
BSCS	Basel Committee of Banking Supervision
CAG	Controller and Auditor General of India
CBS	Core Banking Solutions
CCBs	Central Cooperative Banks
CDs	Certificate of Deposits
CDR	Credit-Deposit Ratio
CFT	Combating the Finance of Terrorism
CMA	Credit Monitoring Arrangement
CP	Commercial paper
CRISIL	Credit Rating Information Services of India Ltd
CRR	Cash Reserve Ratio
CAMEL	Capital Adequacy Asset Quality Management Earning Liquidity
CAR	Capital Adequacy Ratio
CARE	Credit Analysis and Research Limited
C&F	Cost and Freight
C&I	Cost and Insurance
CIF	Carriage, Insurance and Freight
CLB	Company Law Board

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CVC	Central Vigilance Commission
DAP	Development Action Plan
DBOD	Department of Banking Operation and Development
DCCBs	District Central Cooperative Banks
DD	Demand Draft
DFS	Department of Financial Services
DGFT	Director General of Foreign Trade
DIC	District Industrial Centre
DICGC	Deposit Insurance and Credit Guarantee Corporation
DLRC	District Level Review Committee
DPG	Deferred Payment Guarantee
DPN	Demand Promissory Note
DRI	Differential Rate of Interest Scheme
DRT	Debt Recovery Tribunal
DSCR	Debt Service Coverage Ratio
DTL	Demand and Time Liabilities
DBS	Department of Banking Supervision
DCF	Discounted Cash Flow
DEFTY	Dollar Denominated Nifty
DPs	Depository Participants
DPG	Deferred Payment Guarantee
DRIP	District Rural Industries Project
DSR	Debt Service Ratio
ECB	External Commercial Borrowing

ECB	European Central Bank
ECGC	Export Credit Guarantee Corporation
ECS	Electronic Clearing System
EEC	European Economic Community
EFF	Extended Fund Facility
EFT	Electronic Fund Transfer
EMI	Equated Monthly Instalment
EOU	Export Oriented Unit
EPC	Export Promotion Council
EPZ	Export Processing Zone
EWS	Economically Weaker Sections
EXIM Bank	Export Import Bank of India
EEFC	Exchange Earner's Foreign Currency
EFR	Exchange Fluctuation Reserve
ELSS	Equity-Linked Saving Scheme
EPS	Earnings Per Share
FCI	Food Corporation of India
FCNRA	Foreign Currency (Non- Resident) Account
FCNR Scheme	Foreign Currency (Non-Resident) Scheme
FDI	Foreign Direct Investment
FEDAI	Foreign Exchange Dealers Association of India
FERA	Foreign Exchange Regulation Act
FEMA	Foreign Exchange Management Act
FCA	Foreign Currency Asset

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FII	Foreign Institutional Investors
FIPB	Foreign Investment Promotion Board
FIRPS	Foreign Inward Remittance Payment Scheme
FCRA	Foreign Contribution Regulation Act
FC(O)NR Scheme	Foreign Currency (Ordinary) Non-Repatriable Scheme
FCCB	Foreign Currency Convertible Bonds
FOB	Free on Board
FE (FOREX)	Foreign Exchange
FRA	Forward Rates Agreements
GATT	General Agreement on Tariff and Trade
GDP	Gross Domestic Product
GDRs	Global Deposit Receipts
GOI	Government of India
GNP	Gross National Product
GAPP	Generally Accepted Accounting Principles
G-Sec	Government Securities
HUDCO	Housing and Urban Development Corporation Ltd
IBA	Indian Banks' Association
IBRD	International Bank for Reconstruction and Development
ICICI	Industrial Credit and Investment Corporation of India
IDBI	Industrial Development Bank of India
IE Code	Import and Export Code
IFSC	Indian Financial System Code

IFCI	Industrial Finance Corporation of India
IFFCO	Indian Farmer's and Fertilizers Co-op Ltd
IGF	India Growth Fund
ILO	International Labour Organisation
IMF	International Monetary Fund
IS	Information System
IRS	Interest Rate Swap
IT	Information Technology
ICAI	Institute of Chartered Accountants of India
ICC	International Chamber of Commerce
ICRA	Information and Credit Rating Agency of India Ltd
KVIC	Khadi and Village Industries Corporation
KYC	Know Your Customer
LAMPS	Large-size Adivasi Multi-Purpose Society
LDB	Land Development Banks
LIC	Life Insurance Corporation of India
LIBOR	London Inter Bank Offer Rate
LIG	Low Income Group
LAB	Local Area Bank
LAN	Local Area Network
LC	Letter of Credit
LG	Letter of Guarantee
LFAR	Long Form Audit Report
LIBID	London Inter Bank Bid Rate

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MCA	Ministry of Corporate Affairs
MEA	Ministry of External Affairs
MICR	Magnetic Ink Character Recognition
MIG	Middle Income Group
MIS	Management Information System
MOU	Memorandum of Understanding
MPBF	Maximum Permissible Bank Finance
M RTP Act	Monopolies Restrictive Trade Practices Act
MSP	Minimum Support Price
NABARD	National Bank for Agriculture and Rural Development
NAV	Net Asset Value
NBFC	Non-Banking Finance Companies
NEFT	National Electronic Fund Transfer
NOF	Net Owned Funds
NDP	Net Domestic Product
NGO	Non-Government Organisations
NHB	National Housing Bank
NNP	Net National Product
NPA	Non-Performing Asset
NRE	Non-Resident External Account
NRI	Non-Resident Indian
NSE	National Stock Exchange
NSEI	National Stock Exchange India
NSIC	National Small Industries Corporation

NSDL	National Securities Depositor Limited
OECD	Organisation for Economic Cooperation and Development
OGL	Open General Licence
OPEC	Organisation of Petroleum Exporting Countries
PAN	Permanent Account Number
PACS	Primary Agricultural Coop Society
PC	Participation Certificates
PPF	Public Provident Fund
PCL	Packing credit Loan
PMEGP	Prime Minister Employment Generation Programme
PLR	Prime Lending Rate
PMLA	Prevention of Money Laundering Act 2002
PSB	Public Sector Banks
QIS	Quarterly Information System
RBI	Reserve Bank of India
RRB	Regional Rural Banks
RFC	Resident Foreign Currency
RTGS	Realtime Gross Settlement System
SDR	Special Drawing Rights
SEBI	Securities and Exchange Board of India
SLR	Statutory Liquidity Ratio
SSI	Small Scale Industries
SFC	State Finance Corporation

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SIDBI	Small Industries Development Bank of India
SLBC	State Level Bankers Committee
SLR	Statutory Liquidity Ratio
SWIFT	Society for Worldwide International Financial Telecommunications
SHG	Self Help Group
TB	Treasury Bills
TOD	Temporary Overdraft
WOS	Wholly Owned Subsidiary
WTO	World Trade Organisation
Y2K	Year 2000
YTM	Yield to Maturity
UCN	Unique Code Number
WT	Wire Transfer