

Accounting and Auditing Framework

PART A

01. This Chapter discusses the statutory provisions and regulatory requirements affecting the accounts and audit of banks. As provisions relating to accounts and audit of co-operative banks may differ from one State to another, they are not discussed in this Guidance Note.

Form and Content of Financial Statements

02. Sub-sections (1) and (2) of section 29 of the Banking Regulation Act, 1949, deal with the form and content of financial statements of a banking company and their authentication. These sub-sections are also applicable to nationalised banks, State Bank of India, subsidiaries of the State Bank of India, and Regional Rural Banks.

03. Sub-section (1) of section 29 requires every banking company to prepare a balance sheet and a profit and loss account in the forms set out in the Third Schedule to the Act or as near thereto as the circumstances admit. These financial statements have to be prepared as on the last working day of each financial year (i.e., 31st March) in respect of all business transacted during the year. A foreign banking company (i.e., a banking company incorporated outside India and having a place of business in India) has to similarly prepare a balance sheet and a profit and loss account every year in respect of all business transacted through its branches in India. As per Accounting Standard 3, the bank should prepare the cash flow statement also. Hence the financial statements of the bank shall include the cash flow statement along with the balance sheet and profit and loss account as well.

Salient Features of the Third Schedule

04. Form A of the Third Schedule to the Banking Regulation Act, 1949, contains the form of balance sheet and Form B contains the form of profit and loss account. The text of the Third Schedule to the Banking Regulation Act, 1949 is given in **Appendix II** of this Guidance Note.

05. The balance sheet as well as the profit and loss account are required to be presented in vertical form. Capital and liabilities are to be presented under the following five broad heads:

- Capital
- Reserves and Surplus
- Deposits
- Borrowings
- Other liabilities and provisions

06. Assets are required to be presented under the following six broad heads:

- Cash and Balances with Reserve Bank of India
- Balances with Banks and Money at call and short notice
- Investments
- Advances
- Fixed assets
- Other assets

07. Details of items of capital, liabilities and assets are required to be presented in the prescribed form in various schedules.

08. The aggregate amounts of contingent liabilities and bills for collection are to be presented on the face of the balance sheet. While details of contingent liabilities are to be presented by way of a schedule.

09. The following items are required to be presented on the face of the profit and loss account.

- I. *Income*
 - Interest earned
 - Other income
- II. *Expenditure*
 - Interest expended
 - Operating expenses
 - Provisions and contingencies
- III. *Profit (Loss)*
 - Net profit (loss) for the year
 - Profit/loss brought forward
- IV. *Appropriations*

Transfer to statutory reserves

Transfer to other reserves

Transfer to Government/Proposed Dividend

Balance carried over to balance sheet

10. Prescribed details of interest earned, other income, interest expended and operating expenses are required to be given by way of schedules to the profit and loss account.

Disclosures Prescribed by RBI

11. In addition to the disclosures to be made in the balance sheet and profit and loss account in pursuance of the requirements of the Third Schedule to the Act, the RBI has, vide its Master Circular no. DBR.BP.BC No 23/21.04.018/2015-16 dated July 1, 2015 on "Disclosure in Financial Statements – 'Notes to Accounts'", prescribes disclosures to be made in the Notes to Accounts in respect of certain significant aspects of the items of financial statements of banks. The disclosures in connection with Accounting Standards as mentioned in the circular is only the minimum required and other disclosures as prescribed by the Accounting Standards is mandatory to the extent they are not inconsistent with RBI circular.

Disclosures Required Under Accounting Standards

12. The disclosure requirements under the various Accounting Standards, as specified under Section 133 of the Companies Act, 2013, read with Rule 7 of the Companies (Accounts) Rules 2014, in so far as they apply to banking companies or Accounting Standards issued by the ICAI are also to be complied with.

Requirements of the Banking Regulation Act, 1949, vis-a-vis Companies Act, 2013

13. The requirements of the Companies Act, 2013, relating to the balance sheet, profit and loss account and cash flow statement of a company, in so far as they are not inconsistent with the Banking Regulation Act, 1949, also apply to the financial statements, as the case may be, of a banking company [sub-section (3) of section 29 of the Act]. It may be noted that this provision does not apply to nationalised banks, State Bank of India, its subsidiaries and regional rural banks.

14. The Union Budget for 2014-15 emphasised the urgent need for convergence of the current Indian accounting standards with International Financial Reporting Standards (IFRS). The Ministry of Corporate Affairs (MCA), Government of India notified the rules for IFRS converged Indian Accounting

Standards (Ind AS) along with its implementation road map for corporates in a phased manner from 2016-17 onwards. Recently, the following roadmap for Ind AS implementation in case of insurance companies, banking companies and non-banking financial companies (NBFCs) has also been announced:

“Roadmap drawn-up for implementation of Indian Accounting Standards (Ind AS) converged with International Financial Reporting Standards (IFRS) for Scheduled Commercial Banks (Excluding RRBs), Insurers/Insurance Companies and Non-Banking Financial Companies (NBFCs)

In pursuance to the Budget Announcement by the Union Finance Minister Shri Arun Jaitley, after consultations with Reserve Bank of India (RBI), Insurance Regulatory and Development Authority (IRDA) and Pension Fund Regulatory and Development Authority (PFRDA), the following roadmap for implementation of Indian Accounting Standards (Ind AS) converged with International Financial Reporting Standards (IFRS) for Scheduled commercial banks (excluding RRBs), insurers/insurance companies and Non-Banking Financial Companies (NBFCs) has been drawn up:

(I) Scheduled commercial banks (excluding RRBs) and Insurer/Insurance Companies

- (a) Scheduled commercial banks (excluding Regional Rural Banks (RRBs), All-India Term-lending Refinancing Institutions (i.e. Exim Bank, NABARD, NHB and SIDBI) and Insurers/Insurance companies would be required to prepare Ind AS based financial statements for accounting periods beginning from April 1, 2018 onwards, with comparatives for the periods ending March 31, 2018 or thereafter. Ind AS would be applicable to both consolidated and individual financial statements.
- (b) Notwithstanding the roadmap for companies, the holding, subsidiary, joint venture or associate companies of Scheduled commercial banks (excluding RRBs) would be required to prepare Ind AS based financial statements for accounting periods beginning from April 1, 2018 onwards, with comparatives for the periods ending March 31, 2018 or thereafter.
- (c) Urban Cooperative Banks (UCBs) and Regional Rural Banks (RRBs) shall not be required to apply Ind AS and shall continue to comply with the existing Accounting Standards, for the present.

(II) NBFCs

NBFCs will be required to prepare Ind AS based financial statements in two phases:

- (a) Under Phase I, the following categories of NBFCs shall be required to prepare Ind AS based financial statements for accounting periods beginning from April 1, 2018 onwards with comparatives for the periods ending March 31, 2018 or thereafter. Ind AS would be applicable to both consolidated and individual financial statements.
 - (i) NBFCs having net worth of Rs.500 crores or more.
 - (ii) Holding, subsidiary, joint venture or associate companies of companies covered under (a)(i) above, other than those companies already covered under the corporate roadmap announced by the Ministry of Corporate Affairs (MCA), Government of India (GoI).
- (b) Under Phase II, the following categories of NBFCs shall be required to prepare Ind AS based financial statements for accounting periods beginning from April 1, 2019 onwards with comparatives for the periods ending March 31, 2019 or thereafter. Ind AS would be applicable to both consolidated and individual financial statements.
 - (i) NBFCs whose equity and/or debt securities are listed or are in the process of listing on any stock exchange in India or outside India and having net worth less than Rs. 500 crores.
 - (ii) NBFCs other than those covered in (a)(i) and (b)(i) above, that are unlisted companies, having net worth of Rs. 250 crores or more but less than Rs. 500 crores.
 - (iii) Holding, subsidiary, joint venture or associate companies of companies covered under (b) (i) and (b)(ii) above, other than those companies already covered under the corporate roadmap announced by the MCA, GoI.

Unlisted NBFCs having net worth below Rs. 250 Crores and not covered under the above provisions shall continue to apply Accounting Standards specified in Annexure to Companies (Accounting Standards) Rules, 2006 as amended by the Companies (Accounting Standards) Amendment Rules 2016.”

(III) Scheduled commercial banks (excluding RRBs)/NBFCs/insurance companies/insurers shall apply Indian Accounting Standards (Ind AS) only if they meet the specified criteria, they shall not be allowed to voluntarily adopt Indian Accounting Standards (Ind AS). This, however, does not preclude an insurer/insurance company/NBFC from providing Ind AS compliant financial statement data for the purposes of preparation of consolidated financial statements by its parent/investor, as required by the parent/investor to comply with the existing requirements of law.

Draft Notification/Rules, as required, would be issued by the Ministry of Corporate Affairs, RBI and IRDA in due course.”

[Source: Press Information Bureau, Government of India, Ministry of Corporate Affairs, Release ID: 134578, Dated: 18th January 2016]

Banks Listed on a Stock Exchange

15. Banks listed on a stock exchange have to also comply with the requirements of the Listing Agreement as amended from time to time. In respect of securities issued and traded on foreign bourses, if any, the issuer bank has to comply with the applicable regulations of that jurisdiction.

Consolidated Financial Statements in case of one or more Subsidiaries

16. Banks are required to prepare Consolidated Financial Statements incorporating the Financial Statements of all the subsidiaries in the same form and manner as that of its own. In case the Bank is a Company, then such Consolidated Financial Statements shall also be laid before the annual general meeting of the company along with the laying of its financial statement by virtue of sub – section (3) of section 129 of Companies Act, 2013.

Further a separate statement containing the salient feature of the financial statement of its subsidiary or subsidiaries in such form as may be prescribed shall also be attached along with its financial statement.

Notes and Instructions Issued by RBI

17. The RBI has issued notes and instructions for compilation of balance sheet and profit and loss account. These notes and instructions provide an authoritative interpretation of the requirements of the Third Schedule to the Act and are thus useful in preparation of financial statements of banks.

Signatures

18. Sub-section (2) of section 29 of the Act requires that the financial statements of banking companies incorporated in India should be signed by the manager or principal officer of the banking company and by at least three directors (or all the directors in case the number is less than three). The financial statements of a foreign banking company are to be signed by the manager or agent of the principal office in India. It may be noted that the accounts of a branch are usually signed by the manager of the branch and/or the accountant.

19. The provisions of sub-section (2) of section 29 are also applicable to nationalised banks, State Bank of India, its subsidiaries, and regional rural banks.

Auditor's Report

20. In the case of a nationalised bank, the auditor is required to make a report to the Central Government in which he has to state the following:

- (a) whether, in his opinion, the balance sheet is a full and fair balance sheet containing all the necessary particulars and is properly drawn up so as to exhibit a true and fair view of the affairs of the bank, and in case he had called for any explanation or information, whether it has been given and whether it is satisfactory;
- (b) whether or not the transactions of the bank, which have come to his notice, have been within the powers of that bank;
- (c) whether or not the returns received from the offices and branches of the bank have been found adequate for the purpose of his audit;
- (d) whether the profit and loss account shows a true balance of profit or loss for the period covered by such account; and
- (e) any other matter which he considers should be brought to the notice of the Central Government.

21. The report of auditors of State Bank of India is also to be made to the Central Government and is almost identical to the auditor's report in the case of a nationalised bank.

22. The auditor's report in the case of subsidiaries of State Bank of India is identical to the auditor's report in the case of a nationalised bank, except that all references to Central Government have to be construed instead as references to the State Bank of India. Similar is the position in the case of regional rural banks, except that the references are instead to the bank concerned.

Format of Audit Report

23. The auditors, central as well as branch, should also ensure that the audit report issued by them complies with the requirements of SA 700, "Forming an Opinion and Reporting on Financial Statements", and where required with the SA 705, "Modifications to the Opinion in the Independent Auditor's Report" and/or SA 706, "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report", as may be applicable. The auditor should ensure that not only information relating to number of unaudited branches is given but quantification of advances, deposits, interest income and interest expense for such unaudited branches has also been disclosed in the audit report. Such disclosure in the audit report is not only in accordance with the best international trends but also provides useful information to users of financial statements, for example, though the absolute number of unaudited branches might be quite large but in relation to overall operations of the bank such unaudited branches

are quite miniscule and thus, not material. Therefore, the auditor should ensure that the complete information in respect of unaudited branches is collected and disclosed in the audit report.

24. Further, in accordance with the Announcement issued by the Institute of Chartered Accountants of India, the bank branch auditors need to mention the total number of debits/ credits and amounts in the Memorandum of Changes submitted by them, under the Other Matters Paragraph in the their audit report. This would help in ensuring that all adjustments suggested by the branch auditors in the Memorandum of Changes, including those which have not *per se* been accepted by the bank branch managements, have been duly brought to the knowledge of the statutory central auditors. It may be noted that the information in respect of Memorandum of Changes under the "Other Matters Paragraph" would include both such MoCs which have been accepted as well as those not accepted by the bank branch management, though this distinction need not *per se* be brought out in the audit report.

25. An illustrative format of report of the Auditor of a Nationalised Bank is given in **Appendix III** to this Guidance Note.

26. The auditor of a banking company is required to state in his report the followings in terms of provisions of Section 30(3) of The Banking Regulation Act, 1949:

- (a) whether or not the information and explanations required by him have been found to be satisfactory;
- (b) whether or not the transactions of the company which have come to his notice have been within the powers of the Bank;
- (c) whether or not the returns received from the branch offices of the Bank have been found adequate for the purpose of his audit;
- (d) whether the profit and loss account shows a true balance of profit or loss for the period covered by such account; and
- (e) any other matter which he considers should be brought to the notice of the shareholders of the company.

In addition to the aforesaid, the auditor of a banking company is also required to state in his report in respect of matters covered by Section 143(2) & (3) of the Companies Act, 2013.

27. As per reporting requirements cast through Rule 11 of the Companies (Audit and Auditors) Rules, 2014 the auditor's report shall also include their views and comments on the following matters, namely:

- i) whether the bank has disclosed the impact, if any, of the pending litigations on its financial position in its financial statements
- ii) whether the bank has made provision, as required under the law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts
- iii) whether there has been any delay in transferring amounts, required to be transferred to the Investment Education and Protection Fund by the bank

28. An illustrative format of report of the Auditor on the Standalone Financial Statements of a banking company is given in **Appendix IV** to the Guidance Note.

Long Form Audit Report

29. Besides the audit report as per the statutory requirements discussed above, the terms of appointment of auditors of public sector banks, private sector banks and foreign banks (as well as their branches), require the auditors to also furnish a long form audit report (LFAR). The matters which the banks require their auditors to deal with in the long form audit report have been specified by the RBI.

30. The LFAR is to be submitted before 30th June every year. To ensure timely submission of LFAR, proper planning for completion of the LFAR is required. While the format of LFAR does not require an executive summary to be given, members may consider providing the same to bring out the key observations from the whole document.

Reporting to RBI

31. The RBI issued a Circular No. DBS.FGV.(F).No. BC/ 23.08.001/2001-02 dated May 3, 2002 relating to implementation of recommendations of the Committee on Legal Aspects of Bank Frauds (Mitra Committee) and the recommendations of the High Level Group set-up by the Central Vigilance Commission applicable to all scheduled commercial banks (excluding RRBs). Regarding liability of accounting and auditing profession, the said circular provided as under:

“If an accounting professional, whether in the course of internal or external audit or in the process of institutional audit finds anything susceptible to be fraud or fraudulent activity or act of excess power or smell any foul play in any transaction, he should refer the matter to the regulator. Any deliberate failure on the part of the auditor should render himself liable for action”.

32. As per the above requirement, the member shall be required to report

the kind of matters stated in the circular to regulator, i.e., RBI. In this regard, attention of the members is also invited to Clause 1 of Part I of the Second Schedule to the Chartered Accountants Act, 1949, which states that:

“A chartered accountant in practice shall be deemed guilty of professional misconduct, if he discloses information acquired in the course of his professional engagement to any person other than his client, without the consent of his client or otherwise than as required by any law for the time being in force.”

33. Under the said provision, if a member of the Institute *suo motu* discloses any information regarding any actual or possible fraud or foul play to the RBI, the member would be liable for disciplinary action by the Institute. However, a member is not held guilty under the said clause if the client explicitly permits the auditor to disclose the information to a third party. If the above-mentioned requirement of the Circular is included in the letter of appointment (which constitutes the terms of audit engagement) then it would amount to the explicit permission by the concerned bank (client) to disclose information to the third party, i.e., the RBI.

34. Thus, auditors while reporting such a matter to the bank should also report the matter simultaneously to the Department of Banking Supervision, RBI provided the terms of audit engagement require him to do so.

35. Auditor should also consider the provisions of SA 250, “Consideration of Laws and Regulations in an Audit of Financial Statements”. Para A19 of the said Standard explains that the duty of confidentiality may be over-ridden by statute, law or by courts (For example, the auditor is required to report certain matters of non-compliance to RBI as per the requirements of the Non-Banking Financial Companies Auditor’s report (Reserve Bank) Directions, 1988, issued by the RBI).

36. RBI has issued a Master Direction on Fraud no. DBS.CO.CFMC.BC.No.1/23.04.001/2016-17 dated July 1, 2016 on “Frauds – Classification and Reporting by Commercial banks and select FIs” on the matters relating to classification and reporting of frauds and laying down a suitable reporting system. As per the said direction, the primary responsibility for preventing frauds is that of bank management. Banks are required to report frauds to the board of directors and also to the RBI.

37. In the aforesaid context, it may be emphasised that such a requirement does not extend the responsibilities of an auditor in any manner whatsoever as far as conducting the audit is concerned. The requirement has only extended the reporting responsibilities of the auditor. As far as conduct of audit is concerned, the auditor is expected to follow the Standards on Auditing issued by the ICAI and perform his functions within that framework. SA 240, “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements” states that

an auditor conducting an audit in accordance with SAs is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. Members' attention is invited to audit procedures as dealt in Chapter 2, "Risk Assessment and Internal Control" of Part II of the Guidance Note.

38. There are several reporting requirements relating to frauds, if detected, in LFAR and Ghosh Committee recommendations. The auditor should also refer to reports of internal auditors, concurrent auditors, inspectors, etc., which may point out significant weaknesses in the internal control system. Such an evaluation would also provide the auditor about the likelihood of occurrence of transaction involving exercise of powers much beyond entrusted to an official. It must be noted that auditor is not expected to look into each and every transaction but to evaluate the system as a whole. Therefore, if the auditor while performing his normal duties comes across any instance, he should report the matter to the RBI in addition to Chairman/Managing Director/Chief Executive of the concerned bank.

Reporting of Frauds to Central Government under the Companies Act, 2013

39. In case of a banking company, in term of provision of section 143(12) of the Companies Act, 2013:

"Notwithstanding anything contained in this section, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such amount or amounts as may be prescribed, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as may be prescribed:

Provided that in case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as may be prescribed:

Provided further that the companies, whose auditors have reported frauds under this sub-section to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as may be prescribed".

The audit procedure in this regard would be guided by the Guidance Note on Reporting on Fraud under Section 143(12) of the Companies Act, 2013, issued by ICAI.

Audit of Branches

40. Audit of branches of banking companies is required under sub-section (8) of section 143 of the Companies Act, 2013. It is thus obligatory for a banking company to get the financial statements of each of its branch offices audited except where exemption from audit is obtained in respect of certain branches under the guidelines of the RBI issued from time to time.

41. The branch auditor has the same powers and duties in respect of audit of financial statements of the branch as those of the central auditors in relation to audit of head office. The branch auditor's report on the financial statements examined by him is forwarded to the central auditors with a copy to the management of the bank. An illustrative format of report of the branch auditor of a Nationalised Bank is given in the **Appendix V** of this Guidance Note. The branch auditor of a public sector bank, private sector bank or foreign bank is also required to furnish a long form audit report to the bank management and to send a copy thereof to the central auditors. The central auditors, in preparing their report on the financial statements of the bank, deal with the branch audit reports in such manner as they consider necessary. An illustrative format of report of the branch auditor of a Banking Company is given in the **Appendix VI** of this Guidance Note.

42. Some Indian banks also have overseas branches. The audit of financial statements of these branches is usually carried out by an accountant duly qualified to act as an auditor of the branch in accordance with the laws of the country concerned. The form of audit report is usually governed by the laws of the country in which the branch is situated.

Branch Audit *vis-à-vis* Audit at Head Office Level

43. There is a significant difference in the scope of audit at a branch of a bank (conducted by branch auditors) and at head office (conducted by central auditors) as well as other controlling offices such as zonal offices and regional offices (usually conducted by central auditors). This difference stems from the fact that the banking business – receiving deposits and making loans and advances – as well as most other banking services take place at the branch level; in the normal course, the head office and the regional/zonal offices do not conduct any banking business. They are generally responsible for administrative and policy decisions which are executed at the branch level. However, accounting for certain transactions, for example, those relating to treasury

functions (viz., investments, funds management, bill re-discounting) is usually centralised, i.e., carried out at the head office. Specialised activities like merchant banking are carried on by separate divisions which operate at the head office and/or at the large designated branches.

44. The branch auditors furnish their audit reports on the branch financial statements to central auditors. Branch returns (comprising balance sheet, profit and loss account and other information relevant for preparation of financial statements of the bank such as particulars of advances) are also received at the head office from un-audited branches. Audited as well as un-audited branch returns are consolidated at the head office. (In some banks, returns pertaining to a region/zone are sent by the branches to the region/zone concerned and are consolidated there. The returns received from various regions/ zones are then consolidated at the head office.)

45. The central auditors, apart from examining consolidation of branch returns, look into specific matters which are normally not dealt with at the branch level. These generally include the following:

- Depreciation on assets like premises, furniture, fixture, computer assets, UPS etc., where the recording of the relevant fixed assets is centralised at the head office.
- Valuation of investments, and provisions for depreciation in value thereof.
- Provisions in respect of non-performing advances and doubtful elements of other current assets.
- Provision for restructured assets, MTM for fair value etc.
- Provisions for gratuity, pension and other retirement benefits.
- Provision for payment of bonus or ex-gratia in lieu of bonus.
- Provision for Standard Assets.
- Provision for interest on overdue term deposits.
- Provision for interest on saving bank deposits beyond the date upto which interest has been provided at the branch level. [For expeditious finalisation of financial statements of branches, some banks follow the practice of requiring the branches to provide for interest on savings bank deposits based on balances therein as at a cut-off (say, 25th March). The interest for the remaining period is provided at the head office level on an estimated basis.]
- Provision in respect of losses arising from frauds discovered.
- Provision for taxation.
- Provision for audit fee.

- Provisions to meet any other specific liabilities or contingencies, the amount of which is material, for example, provision for revision in pay-scales of employees, provision for foreign exchange fluctuations, etc.
- Transfers to reserves.
- Dividends.
- Any other matter dealt with at the head office.

46. Another area which is of utmost importance for the central auditors in the present-day context is that related to inter-office reconciliation. Such reconciliation is mostly centralised at the head office. Each bank has laid down methods and procedures for reconciling the transactions among the various offices of the bank.

47. SA 600, 'Using the Work of Another Auditor', states that the principal auditor should consider the significant findings of the other auditor. The central auditors have to judge whether the observations appearing in the branch auditor's reports, though considered material at the branch level are material in the context of the financial statements of the bank as a whole.

48. Generally, in case of private sector banks there are no separate branch auditors. The statutory auditors appointed are supposed to carry out the entire audit. RBI requires the auditors to mention about the number of branches visited and the coverage of business in the audit report.

Other Important Provisions Relating to Accounts and Audit

49. Section 31 of the Banking Regulation Act, 1949 requires publication of annual accounts (balance sheet and profit and loss account) and auditor's report thereon in the prescribed manner. It is further required that three copies of the above-referred documents should be furnished as returns to the RBI within three months from the end of the period to which they relate. The RBI can extend the aforesaid period by a further period not exceeding three months. These requirements are applicable to banking companies, nationalised banks, State Bank of India, its subsidiaries, and regional rural banks. The regional rural banks are, however, required to furnish the aforesaid returns to NABARD also.

50. Section 32 of the Act requires a banking company (but not other types of banks) to furnish three copies of its annual accounts and auditor's report thereon to the Registrar of Companies at the same time when it furnishes these documents to the RBI. This is considered compliance with section 137 of the Companies Act, 2013 also.

51. Every banking company incorporated outside India is required by section 33 of the Act, to display, not later than the first Monday in August every year, in a conspicuous place in its principal office and every branch office in India

a copy of its last audited annual accounts. It has to also similarly display its complete audited balance sheet and profit and loss account relating to its banking business as soon as they are available. The aforesaid documents have to be kept displayed until replaced by subsequent corresponding documents.

PART B

Accounting Policies

01. The term 'accounting policies' refers to the specific accounting principles and the methods of applying those principles adopted by an enterprise in the preparation and presentation of financial statements.

02. The view presented in the financial statements of an enterprise of its state of affairs and of the profit or loss can be significantly affected by the accounting policies followed in the preparation and presentation of the financial statements. The accounting policies followed vary from enterprise to enterprise. An accounting policy may be significant because of the nature of the entity's operations even if amounts for current and prior periods are not material. The principle consideration should be whether disclosure of an accounting policy would assist users in understanding how transactions, other events and conditions are reflected in the balance sheet and profits/loss account.

03. Recognising the need for disclosure of accounting policies by banks, the RBI has required all scheduled banks to disclose their significant accounting policies. The accounting policies are required to be disclosed at one place along with the notes on accounts. A specimen form in which accounting policies may be disclosed has also been given by the RBI. The specimen indicates broadly the areas in respect of which the accounting policies followed by a bank should be disclosed. Banks can, however, make necessary modifications to suit their individual needs.

04. The specimen form given by the RBI recommends the disclosure of the fact that the financial statements are prepared on the historical cost basis and conform to the statutory provisions and practices prevailing in the country. Besides, disclosure of accounting policies relating to the following areas is recommended in the specimen form:

- (a) Transactions involving foreign exchange, viz., monetary assets and liabilities, non-monetary assets, income and expenditure of Indian branches in foreign currency and of overseas branches, and profit/loss on pending forward contracts.

- (b) Investments.
- (c) Provisions in respect of doubtful advances.
- (d) Fixed assets and depreciation.
- (e) Staff benefits.
- (f) Significant provisions deducted in computing net profit, e.g., provision for income-tax, provision for doubtful advances, etc.
- (g) Grouping of contingency funds in presenting balance sheet.

05. The specimen form of accounting policies was issued by the RBI in 1991. Since then, the RBI has issued a number of guidelines relating to income recognition, asset classification, provisioning and investments. These guidelines have a profound impact on the accounting policies of banks in the relevant areas. Disclosure of accounting policies formulated by banks to comply with these guidelines is essential to enable the users to properly understand the financial statements. Besides, in the case of banks having overseas branches, the methodology adopted for translating the financial statements of such branches may also constitute a significant accounting policy.

Conformity of Accounting Policies with Accounting Standards

06. The Institute of Chartered Accountants of India (ICAI) issues, from time to time, accounting standards for use in the preparation of general purpose financial statements issued to the public by such commercial, industrial or business enterprises as may be specified by the Institute from time to time and subject to the attest function of its members. The Central Government has notified the Accounting Standards issued by the Institute of Chartered Accountants of India under the Companies (Accounting Standards) Rules, 2006¹. Reference may be made to the Announcement “Harmonisation of various differences between the Accounting Standards issued by the ICAI and the Accounting Standards notified by the Central Government” issued by the ICAI. The following is the list of Accounting Standards issued by ICAI and notified by the Central Government as on 31.12.2016:

AS 1	Disclosure of Accounting Policies
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¹ Rule 7(2) of Companies (Accounts) Rule 2014 has clarified that to facilitate proper administration of the notified sections of the Companies Act 2013, in respect of the Section 133, “Till the Standards of Accounting or any addendum thereto are prescribed by Central Government in consultation and recommendation of the National Financial Reporting Authority, the existing Accounting Standards, notified under the Companies Act, 1956 shall continue to apply.”

AS 2	Valuation of Inventories
AS 3	Cash Flow Statements
AS 4	Contingencies and Events Occurring After the Balance Sheet Date
AS 5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
AS 6	Depreciation Accounting (Since withdrawn)
AS 7	Construction Contracts (Revised-2002)
AS 9	Revenue Recognition
AS 10	Property, Plant and Equipment
AS 11	The Effects of Changes in Foreign Exchange Rates (Revised-2003)
AS 12	Accounting for Government Grants
AS 13	Accounting for Investments
AS 14	Accounting for Amalgamations
AS 15	Employee Benefits (Revised-2005)
AS 16	Borrowing Costs
AS 17	Segment Reporting
AS 18	Related Party Disclosures
AS 19	Leases
AS 20	Earnings Per Share
AS 21	Consolidated Financial Statements
AS 22	Accounting for Taxes on Income
AS 23	Accounting for Investments in Associates in Consolidated Financial Statements
AS 24	Discontinuing Operations
AS 25	Interim Financial Reporting
AS 26	Intangible Assets
AS 27	Financial Reporting of Interests in Joint Ventures
AS 28	Impairment of Assets
AS 29	Provisions, Contingent Liabilities and Contingent Assets

07. Of the above Standards notified under the Companies (Accounting Standards) Rules, 2006², presently, the following standards are not applicable to banks to the extent specified.

- (a) AS 13, "Accounting for Investments", does not apply to investments of banks.
- (b) AS 11, "The Effects of Changes in Foreign Exchange Rates", does not apply to accounting of exchange difference arising on a forward exchange contract entered to hedge the foreign currency risk of a firm commitment or a highly probable forecast transaction. However, it shall apply to exchange differences in respect of all other forward exchange contracts.

08. RBI has issued Circular no. DBOD.No.BP.BC.76/ 21.04.018/2004-05 dated March 15, 2005 and Circular no. DBOD.BP.BC.76/21.04.018/2005-06 dated April 5, 2006, containing the guidelines on compliance with AS 11 (Revised 2003).

Audit of Accounts

09. Sub-section (1) of section 30 of the Banking Regulation Act, 1949 requires that the balance sheet and profit and loss account of a banking company should be audited by a person duly qualified under any law for the time being in force to be an auditor of companies. Similar provisions are contained in the enactments governing nationalised banks [Section 10 of the Banking Companies (Acquisition and Transfer of Undertakings) Act of 1970/1980], State Bank of India [section 41 of the State Bank of India Act, 1955], subsidiaries of State Bank of India [section 41 of the State Bank of India (Subsidiary Banks) Act, 1959], and regional rural banks [section 19 of the Regional Rural Banks Act, 1976]. It is important to note that section 41 of the State Bank of India Act, 1955, specifically provides that the affairs of the bank shall be audited by "two or more auditors".

10. Banks operate through a network of branches. The financial statements of branches (comprising branch's profit and loss account, balance sheet and various returns to head office) are incorporated in preparing the financial statements of the bank as a whole. The requirements of section 30 of the Act and the corresponding requirements of other enactments governing different types of banks, referred above, relate to audit of financial

² Rule 7(2) of Companies (Accounts) Rule 2014 has clarified that to facilitate proper administration of the notified sections of the Companies Act 2013, in respect of the Section 133, "Till the Standards of Accounting or any addendum thereto are prescribed by Central Government in consultation and recommendation of the National Financial Reporting Authority, the existing Accounting Standards, notified under the Companies Act, 1956 shall continue to apply."

statements of the bank as a whole and not to audit of financial statements of branches. The discussion in paragraphs 12 to 18 below & paragraphs 20 to 39 of Part A above is also in the context of audit of financial statements of the bank as a whole. The provisions relating to audit of financial statements of branches are discussed in paragraphs 40 to 48 of Part A above.

11. Further, the members, while carrying out audit of a bank (head office or branches) are required to comply with the Engagement and Quality Control Standards issued by the ICAI.

Qualifications of Auditor

12. According to sub-section (1) of section 141 of the Companies Act, 2013, a chartered accountant or a firm whereof majority of partner practicing in India are qualified for appointment as chartered accountants with their firm name may be appointed as an auditor of a company. Sub-section (2) of aforesaid Act provides where a firm including a limited liability partnership is appointed as an auditor of a company, only the partners who are chartered accountants shall be authorised to act and sign on behalf of the firm. However, the following persons shall not be eligible for appointment as an auditor of a company, namely:

- (a) a body corporate other than limited liability partnership;
- (b) an officer or employee of the company;
- (c) a person who is a partner, or who is in the employment of an officer or employee of the company;
- (d) a person who or his relative or partner-
 - i is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company:

Provided that the relative may hold security or interest in the company of face value not exceeding one thousand rupees or such sum as may be prescribed;
 - ii is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of such amount as may be prescribed; or
 - iii has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its

subsidiary, or its holding or associate company or a subsidiary of such holding company, for such amount as may be prescribed;

- (e) a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed;
- (f) a person whose relative is a director or is in the employment of the company as a director or key managerial personnel;
- (g) a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies;
- (h) a person who has been convicted by a court of an offence involving fraud and a period of ten years has not elapsed from the date of such conviction;
- (i) any person whose subsidiary or associate company or any other form of entity, is engaged as on the date of appointment in consulting and specialised services as provided in section 144.

As per sub-section (4) of section 141 of Companies Act, 2013 where a person appointed as an auditor of a company incurs any of the disqualifications mentioned in sub- section (3) after his appointment, he shall vacate his office as such auditor and such vacation shall be deemed to be a casual vacancy in the office of the auditor.

13. The qualification for appointment as an auditor as prescribed in law are the minimum qualifications and a regulatory authority (or an individual bank) may lay down further conditions to determine the eligibility of a chartered accountant or a firm of chartered accountants for appointment as an auditor. The further conditions (which, of course, must be reasonable) may relate to such matters as experience of the chartered accountant /firm/partners of the firm, staff strength, etc. and may be laid down to ensure that the chartered accountants/firms of chartered accountants appointed as auditors possess the requisite skills and resources to carry out the audit effectively.

Appointment of Auditor

14. As per the provisions of the relevant enactments, the auditor of a

banking company is to be appointed at the annual general meeting of the shareholders, whereas the auditor of a nationalised bank is to be appointed by the bank concerned acting through its Board of Directors. In either case, approval of the RBI is required before the appointment is made. The auditors of the State Bank of India are to be appointed by the Comptroller and Auditor General of India in consultation with the Central Government. The auditors of the subsidiaries of the State Bank of India are to be appointed by the State Bank of India. The auditors of regional rural banks are to be appointed by the bank concerned with the approval of the Central Government.

15. As mentioned earlier, the State Bank of India Act, 1955, specifically provides for appointment of two or more auditors. Besides, nationalised banks and subsidiaries of State Bank of India also generally appoint two or more firms as joint auditors.

Remuneration of Auditor

16. The remuneration of auditor of a banking company is to be fixed in accordance with the provisions of sub-section (1) & (2) of section 142 of the Companies Act, 2013 (i.e., by the company in general meeting or in such manner as the company in general meeting may determine). As per proviso of sub section (1) of section 142 remuneration of the first auditor may be fixed by the Board. Further remuneration under sub-section (1) shall, in addition to the fee payable to an auditor, included the expenses, if any, incurred by the auditor in connection with the audit of the company and any facility extended to him but does not include any remuneration paid to him for any other service rendered by him at the request of the company. The remuneration of auditors of nationalised banks and State Bank of India is to be fixed by the RBI in consultation with the Central Government. The remuneration of auditors of subsidiaries of State Bank of India is to be fixed by the latter. In the case of regional rural banks, the auditors' remuneration is to be determined by the bank concerned with the approval of the Central Government.

Powers of Auditor

17. The auditor of a banking company or of a nationalised bank, State Bank of India, a subsidiary of State Bank of India, or a regional rural bank has the same powers as those of a company auditor in the matter of access to the books, accounts, documents and vouchers. He is also entitled to require from the officers of the bank such information and explanations as he

may think necessary for the performance of his duties. In the case of a banking company, he is entitled to receive notice relating to any general meeting. He is also entitled to attend any general meeting and to be heard thereat on any part of the business, which concerns him as an auditor.

18. It is important to note that under section 10 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970/1980, the auditor of a nationalised bank may employ accountants or other persons at the expense of the bank to assist him in audit of accounts. Similar provisions exist in section 41 of the State Bank of India Act, 1955 and the State Bank of India (Subsidiary Banks) Act, 1959. These provisions are aimed at facilitating the work of auditors of these banks by empowering them to appoint the auditors of branches and are particularly important in the context of the fact that the above enactments do not contain any specific provisions for audit of branches of these banks. This is unlike banking companies where audit of branches is required under sub-section (8) of section 143 of the Companies Act, 2013. It may be noted that the Regional Rural Banks Act, 1976, does not contain any provisions relating to audit of branches. Accordingly, in the case of such banks, audit of branches is also carried out by the auditors appointed for the bank as a whole.