

CHAPTER 12 -AUDIT OF BANKS

Q	Reference	Question	Answer
1	ICAI Module	The functioning of banking industry in India is regulated by the Reserve Bank of India (RBI) which acts as the Central Bank of our country. Explain	<p>The functioning of banking industry in India is regulated by the Reserve Bank of India (RBI) which acts as the Central Bank of our country. RBI is responsible for development and supervision of the constituents of the Indian financial system (which comprises banks and non-banking financial institutions) as well as for determining, in conjunction with the Central Government, the monetary and credit policies keeping in with the need of the hour.</p> <p>Important functions of RBI are issuance of currency; regulation of currency issue; acting as banker to the central and state governments; and acting as banker to commercial and other types of banks including term-lending institutions. Besides, RBI has also been entrusted with the responsibility of regulating the activities of commercial and other banks. No bank can commence the business of banking or open new branches without obtaining licence from RBI. The RBI also has the power to inspect any bank.</p>
2	ICAI Module	“The engagement team should hold discussions to gain better understanding of the bank and its environment, including internal control, and also to assess the potential for material misstatements of the financial statements. All these discussions should be appropriately documented for future reference”. Explain	<p>The engagement team discussion ordinarily includes a discussion of the following matters:</p> <ul style="list-style-type: none"> - Errors that may be more likely to occur; -Errors which have been identified in prior years -Method by which fraud might be perpetrated by bank personnel or others within particular account balances and/or disclosures; -Audit responses to Engagement Risk, Pervasive Risks, and Specific Risks; -Need to maintain professional skepticism throughout the audit engagement; -Need to alert for information or other conditions that indicates that a material misstatement may have occurred (e.g., the bank’s application of accounting policies in the given facts and circumstances).

3	ICAI Module	Write a short note on reversal of income under bank audit	<p>Reversal of Income :</p> <ul style="list-style-type: none"> -If any advance, including bills purchased and discounted, becomes NPA as at the close of any year, the entire interest accrued and credited to income account in the past periods, should be reversed or provided for if the same is not realised. -This will apply to Government guaranteed accounts also. In respect of NPAs, fees, commission and similar income that have accrued should cease to accrue in the current period and should be reversed or provided for with respect to past periods, if uncollected. -Further, in case of banks which have wrongly recognised income in the past should reverse the interest if it was recognised as income during the current year or make a provision for an equivalent amount if it was recognized as income in the previous year(s). -Furthermore, the auditor should enquire if there are any large debits in the Interest Income account that have not been explained. <p>It should be enquired is there are any communications from borrowers pointing out differences in Interest charge, and whether action as justified has been taken in this regard.</p>
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