

Credit Control and other Measures
January 2003

Selected circular issued by the Reserve Bank of India during January 2003 reproduced below:

Ref.No.BSD.IP.RO.13/12.05.01/2002-03 dated January 25, 2003

All the Regional Heads of Urban Banks Department

Inspection under Section 35 of the Banking Regulation Act, 1949 (As Applicable to Co-op. Societies) – Comment on quality of audit

Please refer to our circular UBD No. BSD.1.20/12.05.01/2001-02 dated February 6, 2002 advising that our Inspecting Officers should comment on the ratings given by the Departmental Auditors to Urban Co-operative Banks (UCBs) and that the Inspecting Officers should record a special note if it was observed that the audit ratings given by the statutory auditors to UCBs do not reflect the true picture of their financial position and other affairs. The Joint Parliamentary Committee which enquired into the recent stock market scam and matters relating thereto, has recommended that the RBI in their inspection reports, needs to comment on the quality of audit carried out by the auditors and comment on the handling of the issues by the Board of Directors.

2. It has, therefore, been decided that the Inspecting Officers should critically comment on the contents and coverage of the following aspects in the audit reports and whether the marks are awarded against each of the following parameters in an objective manner and based on facts as revealed from the bank's books of account:

- (i) Deposit mobilisation;
- (ii) Performance under priority sector / weaker section advances;
- (iii) Recovery performance – performance of the bank in taking effective legal action;
- (iv) Compliance with income recognition, asset classification and provisioning norms by the bank;
- (v) Maintenance of cash reserve/liquid assets – Investments (SLR/Non-SLR securities –whether bank's investment transactions are as per guidelines issued by RBI;
- (vi) Reserves/ Provisions to cover erosion in the value of assets;
- (vii) Management of funds – whether bank is making judicious use of funds;
- (viii) Loans and advances - existence of a well laid down system of appraisal of loan / credit proposal, sanctioning of loans, documentation, supervision of credit, large advances, etc.;
- (ix) Working results – Deficiencies, if any, in preparing balance sheet and profit and loss account, etc.;
- (x) Operational efficiency – compliance with RBI directives, default in submission of returns to RBI, submission of compliance to inspection report of RBI and last audit report;
- (xi) Efficiency of management – regularity of holding meetings of the Board / general body, proper maintenance of books of accounts, existence of a proper system of internal check and branch control, etc.;
- (xii) Cases of frauds / embezzlement, if any, taken place in the bank – action taken against persons involved – provisioning against likely losses; and
- (xiii) Comments on propriety of expenditure incurred.

The above instances are only illustrative and the Inspecting Officer may cover other areas relevant to the bank. While the comments on internal audit / concurrent audit may be

incorporated in the inspection report, under the paragraph "internal control", a special note should be recorded on the statutory audit reports.

Observations in respect of the statutory audit reports may be communicated to the Registrar of Co-operative Societies promptly through a letter marked "Confidential".

3. Further, Inspecting Officer should comment on the follow up action taken by the Board of Directors on the deficiencies / irregularities pointed out in the audit report. The Inspecting Officers should also examine the manner in which the audit report has been dealt with, *viz.* placing the audit report before the Board, the follow up action taken on the audit report and whether satisfactory compliance has been furnished to the audit report within the stipulated time, etc.

4. The other instructions contained in our circular dated February 6, 2002 remain unchanged.