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**DEPARTMENT OF COMMERCE SCHOOL OF SOCIAL SCIENCE AND
LANGUAGES VELLORE**

BANKING THEORY AND PRACTICE

J COMPONENT

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PROJECT TITILE: THE STUDY OF BANK AUDIT

UNDER THE GUIDANCE OF

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CHAPTER 1

ABSTRACT

A banking company is required to maintain the books of account in accordance with section 209 of the Companies Act, 1956. Banking generally is a sound internal control system in the day to day transaction. The auditor has to evaluate such system carefully. The fundamental requirement of an audit, as regards reporting on statement of account can be discharged from the examination of the internal checked and verification of assets and liabilities by making a comparison and reconciliation of balance with those in the year and that of amount of income and expenses by application of test checks. The banking regulation act casts greater responsibilities on the directors of banks as compared to those of other companies in the matter of supervision over their working. Therefore, they exercise, or are expected to exercise greater supervision over the affairs of bank. The auditor is entitled to rely on such supervision and to limit his checking to test checks. Most of the bank have their own internal audit or inspection department entrusted with the responsibilities of checking the account of various branches.

INTRODUCTION

A physical inventory check is followed by an auditor's examination or inspection of various books of accounts to ensure that all departments are using the same documented system of recording transactions. It's done to make sure the organization's financial statements are accurate.

Examples of auditing evidence include bank accounts, management accounts, payrolls, bank statements, invoices, and receipts. Good auditing evidence should be sufficient, reliable, provided from an appropriate source, and relevant to the audit at hand.

A bank audit is a formal process in which a bank, credit union, or other financial institution's services, system, financial statements, and/or procedures are reviewed and summarized in a report. Every financial services provider is legally required to conduct audits on a regular basis in order to adhere to laws, regulations, and industry standards.

A bank audit is a process carried out by an auditor appointed by the RBI and ICAI to examine the financial statements of the banking institutions and to determine whether or not the banking concerns are abiding by the laws, regulations, and other governing frameworks that are relevant to them.

How Long Does a Bank audit take?

To ensure that all relevant information is complete, timely, and accurate, bank auditors typically spend about three months looking into a bank's financial activities, risk management processes, system, and procedures.

OBJECTIVES:

- 1) A bank should have appropriate controls to manage its risks including effective segregation of duties, accurate measure and reporting of positions, verification and approval of transactions etc.
- 2) Examination of the bank audit system

- 3) Every banking company is required 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. Form A of the third schedule to banking regulation act 1949 contains the forms of balance sheet and form B contains the form of profit and loss account.
- 4) The act requires that the balance sheet and profit and loss account of a company should be audited by a person duly qualified under any law for the time being in force to be an auditor of companies.
- 5) Bank audit is conducted to prevent risks.

Types of Bank audit:

1. Concurrent Audit:

Banks deals with a large number of transactions on a daily basis whose examination is also necessary on a continuous basis for determining the accuracy of the financial statement. For conducting such audit an external auditor is appointed by the bank known as a concurrent auditor who performs an audit of the transaction on a monthly basis.

2. Internal Audit:

Along with the concurrent audit, banks also perform an internal audit for which they appoint an internal auditor to make a regular check on the financial activities of the bank throughout the year. One of the prominent sectors of internal audits is information system audit which is becoming a necessary part of a banking system with the rapid growth of computerized banking functions and it is important to keep an eye on such system on timely intervals to check their work ability.

3. Statutory Audit:

Statutory audit itself comprises the word statute which means regulation. Thus, it can be understood easily that the statutory audit is a mandatory audit defined under the law or banking Regulation Act, 1949. Under statutory audit ICAI and RBI altogether assigns the banks to an auditor who is generally a practicing-chartered accountant and this auditor performs year-end audit in all branches assigned to them by the ICAI from the end of March to first or second week of April.

Some of the important aspects which should be covered under statutory audit are cash verification, tax-related issues, loan accounts verification. After that, an auditor prepares an audit report defining his opinion on a financial statement for the time under which he has to perform an audit and submit his report.

PROCEDURE TO CONDUCT A BANK AUDIT:

The audit of banks or their branches involves the following stages –

- 1. Initial consideration by the statutory auditor in regards to:**
 - a) Declaration of Indebtedness
 - b) Internal Assignments in Banks by Statutory Auditors
 - c) Planning an Audit of Financial Statements
 - d) Communication with Previous Auditor
 - e) Terms of Audit Engagements
 - f) Initial Engagements
 - g) Assessment of Engagement Risks

h) Understanding the Bank and its Environment

2. Identifying and Assessing the Risks of Material Misstatements

3. Understanding the Bank and Its Environment including Internal Control

4. Understanding the Bank's Accounting Process

5. Understanding the Risk Management Process

6. Engagement Team Discussions

7. Establishing the Overall Audit Strategy

8. Developing the Audit Plan

9. Summarizing the audit plan by preparing an audit planning memorandum

10. Determining the Audit Materiality by considering the relationship between the audit

11. While obtaining an understanding of the bank, the auditor should consider whether there are events and conditions which may cast significant doubt on the bank's ability to continue as a going concern

12. Assessing the Risk of Fraud including Money Laundering

13. Assessing specific risks

14. Assessing the risk associated with outsourcing of activities

15. Responses to the Assessed Risks

16. Reviewing the other reports by taking into account the adverse comments, if any, such as:

a) Previous year's audit reports

b) Latest internal inspection reports of bank officials

c) Reserve Bank's latest inspection report

d) Concurrent / Internal audit report

e) report on verification of security

f) Any other internal reports specially related to particular accounts

g) Manager's charge-handing-over report when incumbent is changed

CHAPTER 2

LITERATURE REVIEW

K. Khurana, (2021) Bank Audit Regulations and Reporting Quality. whether bank reporting quality is affected by bank audit regulations. We find that regulations focusing on auditor qualifications and independence improve the quality of bank reporting using a multi-country panel of publicly traded banks. Contrarily, laws that require more direct supervision of external auditors have little, if any, impact on the accuracy of bank reporting. Further cross-sectional analysis reveals that banks with less independent supervisory regimes are particularly affected by bank audit regulations. After accounting for bank regulations related to financial reporting and disclosure, the adoption of International Financial Reporting Standards, and time-varying institutional characteristics at the country level, our results remain valid. Overall, our findings imply that audit regulations are important and that the type of audit regulation will affect how well bank reports are produced.

Jerry Sun and Guoping, Liu *Journal of Banking & Finance, 2014, vol. 40, issue C, 376-387*. The effectiveness of the audit committee is examined in relation to bank risk-taking and risk management. Our research shows that banks with audit committees with long board tenure have lower total risk and idiosyncratic risk, while banks with active audit committee members have higher total risk and idiosyncratic risk. These imply that high audit committee effectiveness might prevent banks from taking unnecessary risks. In line with the idea that effective audit committees may boost risk management efficiency, we also discover that firm performance is more positively correlated with bank risk for banks with long board tenure, a higher proportion of female audit committee members, or larger audit committees than for other banks. However, because it is in conflict with the findings regarding audit committee busyness, this finding should be interpreted with caution.

Dahl, Drew, 2013. "Bank audit practices and loan loss provisioning,". I empirically investigate how loan loss accounting has changed across banks that are categorically different in terms of external auditing procedures. I find evidence of convergence in the target ratios of provisions for loan losses to nonaccrual loans across audit categories using a partial adjustment model and a sample of 75,505 observations on affiliated banks from 1995 to 2009. This is consistent with a

standardized approach to "impaired" loan accounting. On the other hand, I see less convergence in the target ratios of loan to provisions for loan losses, which seems to allow for some managerial discretion.

Boo, E. F., & Sharma, D. (2008). The association between corporate governance and audit fees of bank holding companies. the impact of the board and audit committee's performance on the audit fees in the context of Pakistan's developing nation. We use data from KSE-100 index companies listed on the Pakistan Stock Exchange going back five years. We employ Partial Least Square based Structural Equation Modeling to make the inference. We discover a positive correlation between effective board quality and external auditor fees. According to this finding, a high-quality board should demand a higher-quality audit in order to have more assurance regarding the accuracy of the financial reporting. A high-quality audit committee will ensure reliable financial reporting, which will reduce the efforts of external auditors and result in lower audit fees. This is supported by our discovery that audit committee effectiveness (measured by audit committee size) reduces the external audit fee.

Lee, G. H. (2008). Rule-based and case-based reasoning approach for internal audit of bank. Internal audits are currently very important to banks in order to lower risks, avoid insolvency, and respond quickly to financial incidents In this study, we present an integrated rule-based and case-based audit approach that consists of two stages of reasoning, namely the rule-based reasoning-based screening stage and the case-based reasoning-based auditing stage. Induction rules are used in rule-based reasoning to determine whether or not a new problem require further investigation. Case-based reasoning uses similarity-based matching to locate the case in the case base that most closely resembles the new problem. The method is used with data from a bank's internal audits.

Fields, L. P., Fraser, D. R., & Wilkins, M. S. (2004). An investigation of the pricing of audit services for financial institutions. We look into financial institution audit pricing. By adding risk and complexity measures that are either specific to or more pertinent for banks and that are used by bank regulatory bodies, we alter the typical audit fee model for industrial companies. We find that audit fees are higher for banks with more transaction accounts, fewer securities as a percentage of total assets, lower levels of efficiency, and higher levels of credit risk for a sample of 277 financial institutions in fiscal 2000. Additionally, higher fees apply to savings institutions, banks that engage in more acquisition activity, and institutions that are required to maintain higher risk-adjusted capital levels by regulatory bodies. Future regulatory changes that place a greater

emphasis on market discipline in regulating bank risk-taking are likely to increase the significance of the audit process for banks.

Siddiqui J and Podder J (2002) - "Effectiveness of bank audit in Bangladesh". The effectiveness of financial audits of Bangladeshi banking companies is investigated in the study. Additionally, the reach of bank audits has been looked at. 14 sample banking companies audited financial statements have been taken into consideration. Seven sample companies are identified in the study as having inflated their profits. Despite this, the companies that audited those financial statements did not produce qualified audit reports. The level of independence, objectivity, and competence of the auditors tasked with auditing banking companies is thus called into question by the study.

West, B. P. (2001). On the social history of accounting: The Bank Audit by Bruce Marshall. There is still little research on the social negotiation processes that approve of the increased occupational authority of professions. The complexity of professional services as it is typically defined, however, points to the value of more discursive methods over objective assessments of occupational competence. As a result, items that were once likely to be written off as mere professional trifles may now play a crucial role in the construction of status and image. It is suggested that accounting historians search for and examine the wide variety of texts and other sources that illuminate the frequently fascinating interface between this profession and the larger society in which it is constituted in order to revitalize the development of the social history of accounting.

Walther, J. B. (1988). Communication satisfaction in the bank: An audit evaluation. The Greek Banking Organization's employees were measured for job satisfaction, role conflict, and autonomy. The regulatory impact of autonomy in the aforementioned relationship is also being examined, along with the investigation of the relationship between role conflict and the dimensions of job satisfaction. The Employee Satisfaction Inventory- ESI was used in the current study to measure job satisfaction. Greek employees served as a sample for the inventory's creation. It contained 24 items that assessed six aspects of job satisfaction: Working conditions, pay, promotions, pay, the work itself, the immediate superior, and the organization as a whole are the top six factors. The Role Questionnaire was used to measure role conflict.

Jeffrey, C. (1992). The relation of judgment, personal involvement, and experience in the audit of bank loans. The study investigates and analyses how knowledge and experience affect the auditor's decision-making. Because it covers all phases of the audit process, involves numerous

interests, and establishes the standard and nature of the decisions to be made, judgement auditors become interesting. samples taken from 331 State auditors in Indonesia as of June 2015, divided into six functional roles. Data collection methods, including surveys and stratified sampling, are disproportionate. The findings demonstrated that the main components of competency—knowledge and experience—had a positive impact on the auditor's professional judgement. The outcomes of empirical research also showed that the judgement auditor is more influenced by experience than by knowledge.

CHAPTER-3

METHODOLOGY

The Research methodology includes the various techniques involved in the collection of the data through google forms and presenting it in Tabular form, pie chart and the diagram representation of the collected Data.

RESEARCH DESIGN:

The Research design refers to the strategies and the various components which are integrated to the project. The required data is collected through Questionnaire which was sent digitally through google forms. We shared the link of the forms with our family and friends and got their responses.

SAMPLING DESIGN:

The Sampling can be defined as the study of the unknown population on the basis of a proper representative sample drawn on it. The sample size must mandatorily be large, in fact larger the sample size, the better revealing the identity of the Population.

DATA COLLECTION:

The term ‘data’ as quantitative information about some particular characteristic under consideration. The collection of data plays a major role for any statistical Analysis. The collection of Data can be classified into

- **Primary Data→**

Primary data is the data that is collected for the first time through personal experiences or evidence, particularly for research. It is also described as raw data or first-hand information. The

mode of assembling the information is costly, as the analysis is done by an agency or an external organization, and needs human resources and investment.

- **Secondary Data →**

Secondary data refers to data that is collected by someone other than the primary user. Common sources of secondary data for social science include censuses, information collected by government departments, organizational records and data that was originally collected for other research purposes.

PERIOD OF STUDY:

The Period of study includes the time period in which the study has been made. The study is made between the periods of September to November.

SAMPLING TECHNIQUES:

There are major 2 categories of sampling techniques→

- **Probability sampling→**

The probability sampling method utilizes some form of random selection. In this method, all the eligible individuals have a chance of selecting the sample from the whole sample space. This method is more time consuming and expensive than the non-probability sampling method. The benefit of using probability sampling is that it guarantees the sample that should be the representative of the population.

- **Non-probability sampling→**

The non-probability sampling method is a technique in which the researcher selects the sample based on subjective judgment rather than the random selection. In this method, not all the members of the population have a chance to participate in the study.

The simple random sampling method is used in this research because the questionnaire was prepared digitally and it was circulated so we don't know who may answer the form and all the sections of the society has an equal chance of responding to the questionnaire.

LIMITATIONS OF THE STUDY:

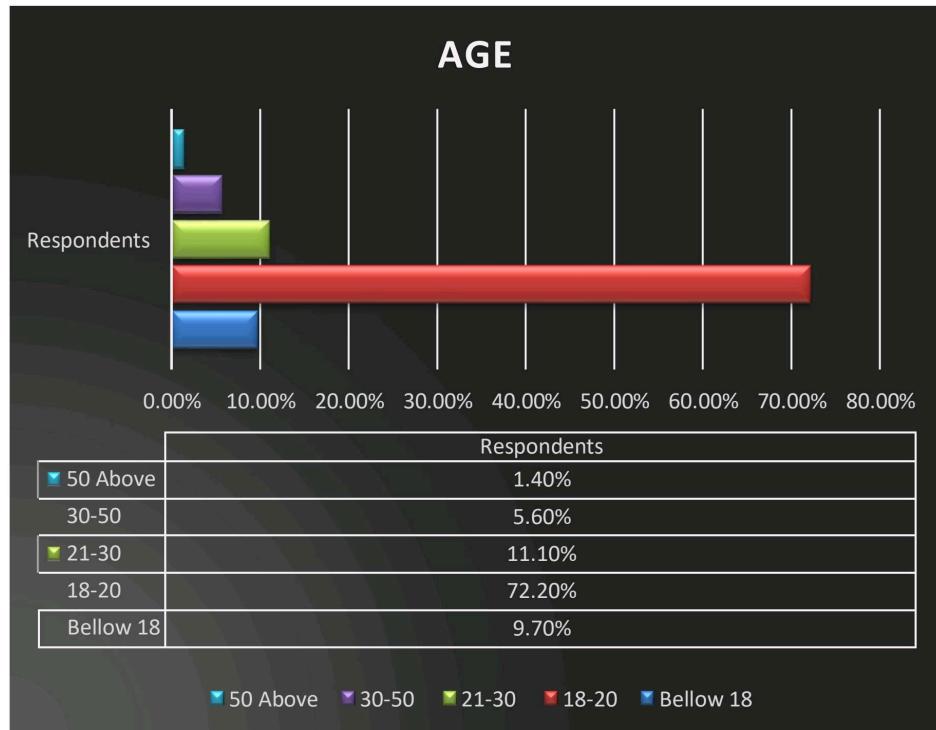
The Satisfaction cannot be measured in terms of units, and there are no prominent ways that enable us to find out the level of satisfaction. And the response we got was not what we expected. We got only limited responses. And also, the most of the people who responded to this form is from the age group of 18-20 so it may affect the data very minutely, but it won't manipulate the data.

CHAPTER-4

DATA ANALYSIS AND ITS INTREPRETATION

Through the primary source we collected the related information through Google forms and the suggestions given by the friends. Here the data as follows.

AGE:

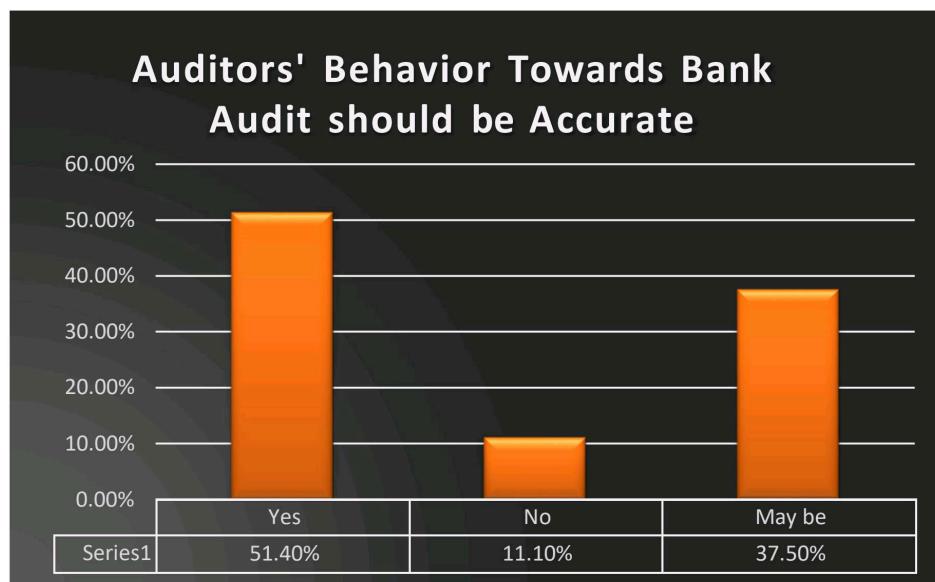


Interpretation:

We have got total of 72 respondents.

These responses were collected from various age group people. 72% of respondents between the age of 18-20 remaining 28% are 21-30, 30-50,50 above.

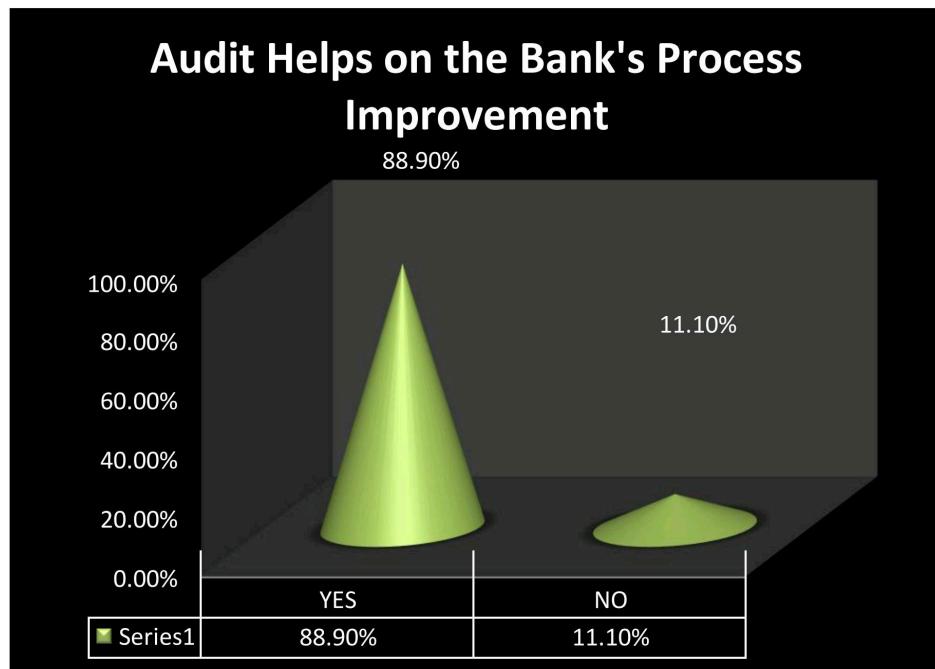
Do you consider the auditors' behavior towards bank audit should be accurate?



Interpretation:

Here we are able to analyze that maximum no. of people are we consider the auditors' behavior towards bank audit should be accurate. Around 51% were consider the auditors' behavior towards bank audit and others are may be or no.

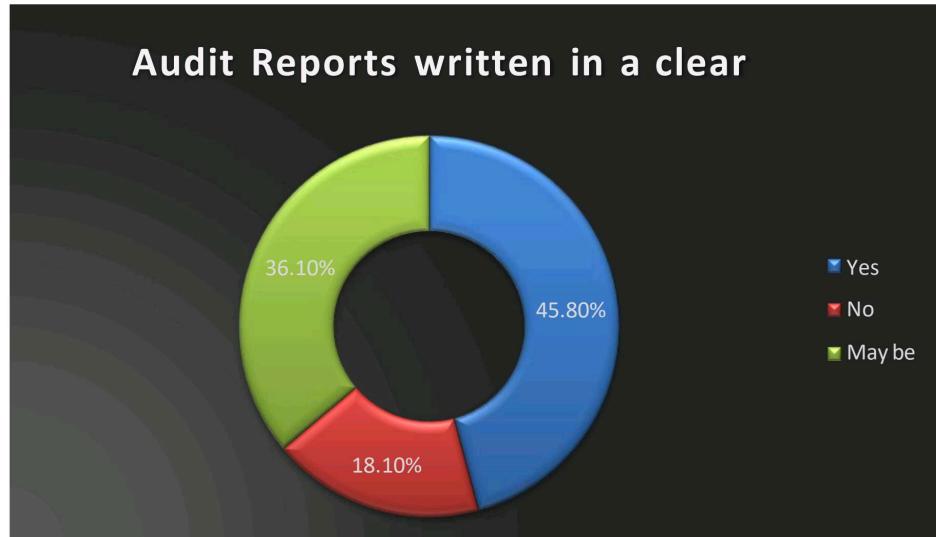
Do you think the audit helps on the bank's process improvement?



Interpretation:

Most of the respondents said that audit helps on the bank's process improvement about 88.90% and 11.10% they said that it not improvement.

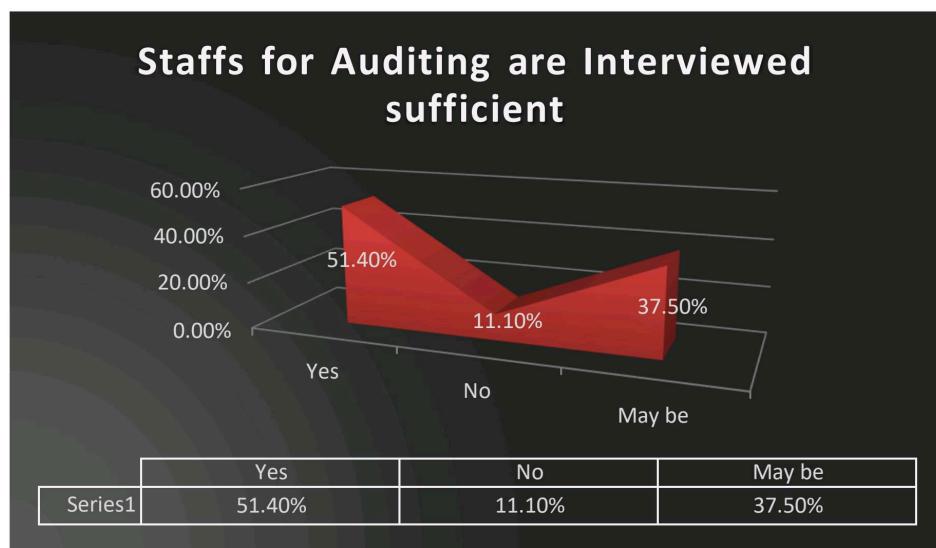
Are Audit reports written in a clear and concise way?



Interpretation:

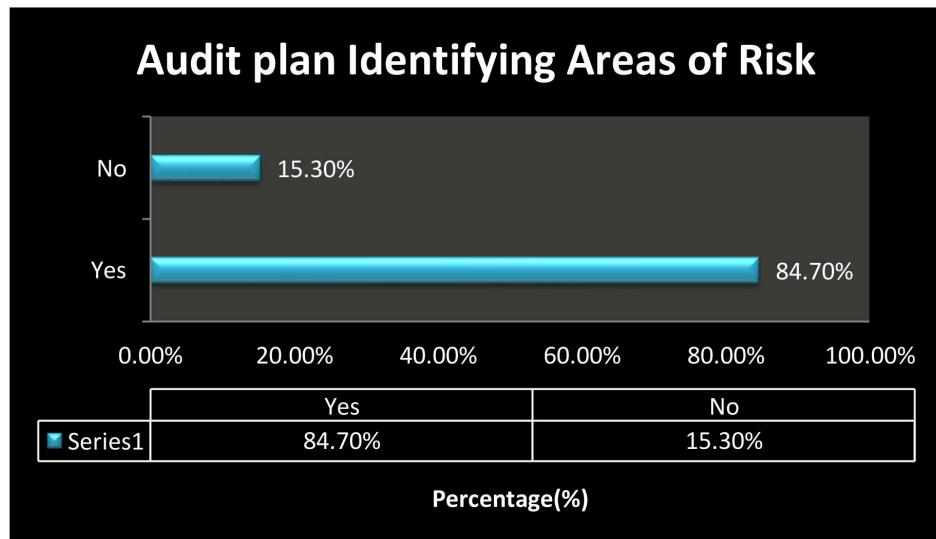
Here we are able to analyze that maximum no. of people are Audit reports written in a clear and concise way. Around 45.80% were Audit reports written in a clear and others are may be 36.10% or no 18.10%.

Do you think that the staffs for auditing are interviewed sufficient for their work?



Interpretation:

Here we are able to analyze that maximum no. of people are think that the staffs for auditing are interviewed sufficient for their work. Around 51.40% staffs for auditing are interviewed sufficient and others are may be 37.50% or no 11.10%.

Has the auditor devised an overall audit plan identifying area of risk?**Interpretation:**

Most of the respondents said that auditor devised an overall audit plan identifying area of risk about 84.70% and 15.30% they said that it not improvement.

CHAPTER-5

SUGGESTIONS AND CONCLUSION

The project the position of Indian banking system as well as the principal laid down by the Basel Committee on banking supervision. This assessment was done in seven major areas, which are core principals, concurrent audit, internal audit, deposit, loan accounting and transparency and foreign exchange transaction. The project concluded that, given the complexity and development of Indian banking sector, the overall level of compliances with the standards and codes is of high order. This project gives the correct ideas about how the major areas can be found by way of effective auditing system i.e. errors, frauds, manipulation etc. from this auditor get the clear ideas how to recommend on the banks position. Project also contain that how to conduct of audit of the banks, what are the various procedure through which audit of banks should be done. From auditing point of view, there is proper follow up of work done in every organization whether it is banking company or any other company or another company there no misconduct of transactions is taken places for that purpose the auditing is very important aspect in today's scenario form company and point of view.