ICAI for branch-level audit of private sector banks

Banking and accounting regulators don't see eye to eye, as RBI wants the practice relaxed even for public sector banks.

Private sector banks may have their branches statutorily audited by an RBI-approved panel, on the pattern of public sector bank audits, if the central bank accepts a suggestion by the Institute of Chartered Accountants of India (ICAI).

The ICAI fears a high incidence of corporate debt restructuring may affect banks' financial health, the level of which cannot always be detected at the aggregated level. The accounting regulator has asked the RBI (Reserve Bank of India) to introduce a mandatory audit of private sector bank branches by people chosen from a central bank-approved panel.

Though mandatory for all public sector banks, such independent audits at the branch level are not required for private banks. Currently, the statutory auditor of private banks conducts branch audits, only if a need is felt to do so.

Ironically, the suggestion comes at a time when the RBI is talking of relaxing audit norms for public sector banks. At the ICAI's recent western region conference, RBI Governor D Subbarao had said, "With concepts like core banking and centralised record keeping, the relevance of the audit of branches of public sector banks has significantly declined." He had said these banks had represented to the RBI that branch audits should be reduced.

"There is merit in this suggestion, since currently the cost of audit of public sector banks is significantly higher than the cost of audit of comparable private sector banks. However, the institute has been resisting this because it would mean a reduction in work for its members," Subbarao had said.

However, ICAI President G Ramaswamy said, "An independent audit of bank branches, both in the public sector as well as private, is essential due to the large amount of corporate restructuring taking place these days. A system generated, auto-alert mechanism may not be fool-proof as physical inspection is essential for identification of non-performing assets (NPAs)." According to RBI data, gross NPAs of private banks stood at Rs 17,972 crore at the end of March 2011, accounting for 2.45 per cent of their gross loans.

The ICAI has made a recommendation to bring the private bank audit system on a par with that of public sector banks to an RBI working group specifically looking into the matter. According to Ramswamy, the collapse of Global Trust Bankover a decade ago happened because the statutory auditors were unable to assess the health of the bank through a central audit. "They did not realise what was going on at the branch level," he said.The Ramesh Gelli-promoted GTB collapsed in 2004, following which it was merged with the Delhi-based Oriental Bank of Commerce.

Facing adverse financial conditions, companies in civil aviation, retail, power and textiles, etc have either got their debts recast by banks or are in the process of doing so. In real estate, corporate debt restructuring has not been allowed after several instances of recast took place during the 2008-09 crisis period. But,
loan restructuring is happening in the sector. In a corporate debt recast, loans are taken as standard assets and not as bad ones.

The ICAI has, meanwhile, favoured a relaxation for companies in terms of not showing their losses due to currency exchange fluctuations in profit and loss accounts for the time being. It wanted the relaxation expired last year to be extended.

Until 2005, the RBI used to directly appoint statutory auditors in public sector banks. Since then, it has been allowing bank boards to select their preferred auditor from an RBI-approved panel of audit firms. The ICAI had criticised the practice, saying it left auditors at the mercy of bank boards and compromised their independence. The RBI is yet to change its position with respect to this autonomy to public sector banks.

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