STATUTORY AUDIT OF BANK TREASURY

Audit of an integrated treasury is a complex task requiring high level of skills, knowledge of market practices and the relevant regulatory environment. Treasury income constitutes a significant portion of a bank's income, many a time equal to the entire income received from advances and the extensive branch network of banks. This paper makes an attempt to highlight the products and market practices in vogue which an auditor of an integrated bank treasury operation will have to be aware of, the relevant regulatory standards, the valuation methods applicable, terminologies used that he has to be familiar with and then proceeds with broad guidelines for evaluation of internal controls (including those relating to information systems). A model audit program that can be tailor made to suit individual needs has also been attempted. The paper also deals with certain risk management practices currently in vogue.

Many banks have set up integrated treasuries, encompassing both rupee and forex denominated transactions. An integrated approach to treasury management involves a common dealer or desk dealing in both domestic and forex financial markets. This enables the bank to optimize its funding and fund deployment and take advantage of arbitrage opportunities between these markets Treasury income constitutes a significant portion of a bank's income, many a time equal to the entire income received from advances and the extensive branch network of banks. Treasury operations are invariably of high value and due to the very nature of its operations, are susceptible to manipulation, fraud or error and consequently to the various types of risks envisaged by Auditing and Assurance Standards (AAS) 6.

—Shyam Ramadhyani

Knowledge of business (AAS 20)

Knowledge of business of a bank treasury is usually low, even in an enlightened community like Chartered Accountants. Consequently, it is important to acquire a thorough knowledge of the products in vogue in the market, market practices, the permissible valuation methods, the regulatory standards prescribed by the Reserve Bank of India (RBI), Foreign Exchange Dealers Association of India (FEDAI) and Fixed Income Money Market and Derivatives Association (FIMMDA), the processes followed by the bank, internal controls exercised, information systems used etc. An idea of the types of trades, settlements, instruments in vogue, certain operational issues relating thereto, principles of valuation etc are set out in the ensuing paragraphs for general understanding.

Types of trades

Customer trades: These are deals

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between the bank and its customers, predominantly in foreign exchange. The profit or loss to the bank is the spread between its inter-bank buying rate and the selling rate to the customer. For example, a customer may place an order to buy USD 100,000. The Bank buys @ Rs.47.98 in the market and sells @ Rs.48.00 to the customer, making a profit of Re.0.02.

Proprietary trades: These are trades by the bank for its own account. They could be in the domestic or overseas market. Buying G-Sec for trading portfolio, in the expectation that price will go up (i.e., interest rates will fall) is an example of a proprietary trade in the domestic market. Buying US dollars and selling Japanese Yen is a cross-currency trade to profit from US dollar appreciation. Proprietary trades are done in the inter bank market.

Trading systems

Negotiated Dealing System (NDS): NDS is an electronic platform for facilitating dealing in government securities and money market instruments. NDS will facilitate electronic submission of bids/ application by members and provides a seamless interface to Securities Settlement System (SSS) of Public Debt Office, RBI. All outright and Repo transactions in treasury bills and dated securities are settled through NDS.

Electronic Trading System (ETS): Bids, offers and quantities are displayed on a screen in descending/ ascending order of price to buy/ sell. The trader enters his order to buy/ sell, quantity and price. If the order is within the live range of buy/ sell prices and quantity, it will be executed instantaneously.

Over-the-counter (OTC): Deals are struck with counter parties on phone and the same is later confirmed in writing. Forex trading is not centralized on an exchange, as in the case of stocks and futures markets. The forex market is considered an over the counter (OTC) or Inter bank market, since transactions are conducted between two counter parties over the telephone or via an electronic network.

Channels

Transactions could be directly with a counter party or through an intermediary, involving intermediation fees.

Settlement

Settlement of transactions takes place by transfers of money between the two parties. The day on which these transfers are effected is called the settlement date

- Takes place T+X days after trade. X could be 0 or more depending on market practice or regulatory requirements.
- **Negotiated Dealing system (NDS):** already explained earlier
- **Delivery Vs. payment:** There is simultaneous exchange of payment and delivery of securities (physical or demat).
- **Electronic settlement:** Foreign exchange deals are settled electronically with credits/ debits to Nostro accounts and take place through SWIFT for transfer of funds.

Types of transactions and settlement dates (forex)

Depending on the time elapsed between the transaction and settlement dates, forex transactions can be categorized into:

Cash Contracts: Settlement date is the same day.

TOM Contracts: Settlement date is the next business day.

Spot transactions: Settlement date is usually two business days ahead.

Forward transactions: Settlement date to be fixed by the parties.

Swaps: Simultaneous sale and purchase or purchase and sale of two currencies in the spot and forward markets, i.e., the first leg is spot and the second leg is forward. The transaction may or may not be with the same counter party. Rationale may be arbitrage.

Cash Reserve Ratio & Statutory Liquid Ratio

SLR: Recognising the need to maintain the confidence of the public in the banking system, the Banking Regulation Act stipulates that every bank shall maintain in cash, gold or unencumbered approved securities, an amount which shall not, at the close of business on any business day, be less than 25% of its 'Demand and Time Liabilities' in India as on the last Friday of the second preceding fortnight.

CRR: Cash reserve by way of balance in a current account with RBI or by way of net balance in current accounts a sum equivalent to 5% of its 'Demand and Time Liabilities' in India as on the last Friday of the second preceding fortnight to be maintained by every bank.

Call/Notice/Term Money

Call money is overnight borrowing or lending in the inter bank money market. Notice money is borrowing or lending in the reporting fortnight. Term money is borrowing or lending for maturities beyond the reporting fortnight. These are resorted to meet SLR and CRR

requirements as well deployment of short-term funds.

Money market lending for more than 14 days are not classified under this head, but are classified as 'Deposits' or 'advances' depending on the nature of lending and the parties to whom the money has been lent.

Banks cannot pay any brokerage on call loans and deposits, except to the extent specified in paragraph 8(e) of the RBI's circular dated July 22, 1974.

Interest bearing and discounted instruments

Government securities, which carry an obligation to pay interest at specific dates, are called interest-bearing securities. On the other hand, discounted instruments do not carry any interest but are purchased at a discount to the redemption value. Examples of discounted instruments are zero coupon bonds, certificate of deposits, treasury bills. Treasury bills may be for different tenors (91/181/364 days etc.)

Repos: Repos involve borrowings from a counter party against pledge of securities to be repurchased at a predetermined date/ rate of interest. They are called reverse repos from the perspective of the lender.

Stock lending and borrowings: These involve lending of securities between two counter parties to be returned at a predetermined date/ rate of interest.

Derivatives

Derivatives offer banks the opportunity to hedge financial risks. Its value is determined by the value of the underlying instrument to which it relates.

Different forms of derivative contracts, include:

Forward contracts: It is an agreement between parties to buy/ sell a specified quantity of an asset at a predetermined mutually agreed date/ price/quantity.

Options: An option is a derivative transaction where the buyer has an option (and not an obligation) to buy/ sell an underlying asset at a specified price on or before a specified future date, by paying a premium. Option may be plain vanilla or exotic (specifically structured) contracts.

Types of Options: An option contract, which can be exercised at any time before expiration date is called as an American Option. A contract, which can be exercised only on the expiration date, is called an European Option**.** European options are generally traded in India.

Call and Put Options: A *call option* gives the buyer of option the right (but not the obligation) to buy an underlying asset for a specified price whereas a *put option* gives the buyer of option the right (but not the obligation) to sell an underlying asset for a specified price.

The *specified price* is known as the *strike/ exercise price* and the *specified date* is known as the *exercise/ expiration date*.

Cap, Floor and Collar: Limit can be set on the strike price for an option contract. If an upper limit on the strike price is set, it is called a *Cap*. If a lower limit if fixed, it is called as the *Floor*. If a combination of both Cap and Floor is used, it is called a *Collar***.** If the market price on the maturity date is higher than the cap, then cap will be the strike price. Similarly if the market rate is lower than the floor price, then floor price will be the strike price. Consequently, in case of Collar, the strike price will be between the cap and floor price.

Futures: They are in the nature of forward contracts but are dealt with on stock exchanges

Swaps

A swap is a contract where by parties agree to exchange obligations that each of them have under their respective underlying contracts.

- *Major types of Swap:*
- Interest Rate swaps
- Currency swaps

A standard *fixed-to-floating interest rate swap* is an agreement between the two parties in which each party contracts to make payments to the other on particular dates in the future till a specified termination date. The first party (*fixed ratepayer)* makes payments at a fixed rate of interest on a notional mutually agreed amount. The other party (floating *ratepayer)* makes payments, at a rate calculated with reference to a bench marked rate, say a six months LIBOR.

Currency swaps involve exchange of currencies at specified exchange rates.

There could be complex instruments involving a combination of the above two types of swaps.

SUMMARY OF TYPES OF INSTRUMENTS

Money market	Government securities (interest bearing and discounted instruments), call money deposits, Repos and liquidity adjustment facility from RBI, commercial paper, certificate of deposits.
Capital market	Shares, convertible debentures, warrants
Debt	Corporate debt papers (fixed or floating rate of interest)
Derivatives	Futures, options, swaps

Some operational aspects (Forex)

Banks enter into correspondent relationship with banks in other countries and sign formal agreements (ISDA) with them. Such agreements would broadly specify the kind of transactions they can handle for the correspondent, the monetary ceiling on such transactions, procedures for settlement, the names and designation of authorized signatories and the terms of the relationship.

There is a reporting requirement of transactions at specified intervals, to the RBI by means of 'R' returns.

Terms used in forex transactions

Forward rate pricing: The exchange rate at which a currency is bought or sold against another currency for delivery and settlement on a future date is called the forward rate. Theoretically, when there is no impediment to capital flows, the forward exchange rate between two currencies differs from the spot rate exactly to the extent of the interest differential between the two countries to which currencies relate.

In general, a currency will be at a premium against another currency in the forward market if the first country's interest rate is lower than that of the second. Conversely, the higher interest rate country's currency will be at a forward discount to that of the lower country's currency.

Nostro and Vostro Accounts: An account maintained by a bank with a foreign bank is called its NOSTRO Account (i.e., Our account with you). Conversely, if a foreign bank were to deal in a local currency of another country, it would maintain a VOSTRO Account (i.e., Your account with us).

Net open positions: Forex risk of a bank is basically determined by the net open positions, which refers to the uncovered currency positions or gaps taking into account all relevant assets and liabilities/ unmatured spot and forward contracts in a particular currency.

Long or short positions: A net position with excess of assets and purchases over liabilities and sales is referred to as long positions. Converse of it, is short position.

Daylight/Overnight limits: The maximum open position in each currency that may remain uncovered during the course of the day is referred to as day light limit. Net open position at the close of business on each working day is referred to as the Overnight limit.

Categorisation/Classification of investments

Investments of banks are categorised into SLR and non-SLR securities. SLR securities are securities notified by RBI for reckoning SLR to be maintained by banks.

The investment portfolio of banks should be classified under three categories viz 'Held to maturity (HTM)', Available for sale (AFS)' and 'Held for Trading(HFT)'. However, in the balance sheet, the investments will continue to be disclosed as per the Banking Regulations Act.

Banks should decide the category of the investment at the time of acquisition and the decision should be recorded on the investment proposals.

HTM Securities acquired by banks with an intention to hold them up to maturity will be classified under HTM. They should not exceed 25% of the bank's total investments, subject to an one time exception permitted by circular dated September 2, 2004 referred to below.

Recapitalization bonds received from Government of India, investment in subsidiaries, joint ventures, debentures/ bonds, which are in the nature of advances, would also be classified under HTM category, but will not be counted for the purpose of ceiling specified for this category.

HFT: Securities acquired by the bank with an intention to trade by taking advantage of short-term price/ interest rate movements will be classified under HFT category. These securities are to be sold within 90 days.

AFS: Securities not falling in the above two categories are classified under AFS category.

Shifting among categories

To be in accordance with the RBI guidelines, which are briefly as follows:

- Shifting to/ from HTM will normally be allowed once at the beginning of the financial year.
- Shifting from AFS to HFT.
- Shifting from HFT to AFS is not generally allowed. Under exceptional circumstances like not being able to sell a security within 90 days due to tight liquidity or extreme volatility or market becoming unidirectional, transfers are permitted.
- All transfers to be approved by the Board of Directors/ ALCO/ Investment committee.
- Transfer from one category to another, under all circumstances, should be done at the acquisition cost/ book value/ market value on the date of transfer, whichever is least, and the

depreciation, if any, on such transfer should be fully provided for.

- A one time shifting of SLR securities not exceeding 25% of the bank's demand and time liabilities as of the last Friday of the second preceding fortnight to HTM category has been permitted by the RBI (refer circular dated September 2, 2004)

Valuation of Investments

It may be noted that AS 13 (Accounting for Investments) do not apply to banks.

Cost of investments

- Incidental charges (example brokerage) not to be included in the cost of AFS and HTM securities;
- Charging of broken period interest (interest accrued up to the time of acquisition on the securities purchased) to the Profit and Loss account.
- Front-end fees, upfront fees and underwriting commission received in respect of securities devolved are to be generally reduced from the cost of the security.

Recognition of Income

- Debentures/ bonds are subject to appropriate provisioning/ de-recognition of unrealized income, in line with the prudential norms.

Profit or loss on sale

- To be determined using weighted average or first in first out method.
- Profit on sale of investments in HTM category should be taken to the Profit & Loss Account and thereafter be appropriated to Capital Reserve. Loss on sale will be recognized in the Profit & Loss account.
- Profit or Loss on sale of investments in HFT and AFS categories will be taken to the Profit & Loss Account.

Valuation

Mode of valuation	Security type
Acquisition cost, unless it is more than the face value, in which case premium is amortized over the period till maturity.	HTM
Valued at market price, scrip wise as per quotations received from FIMMDA. Depreciation/appreciation to be aggregated classification wise in each category. Net depreciation to be provided and net appreciation to be ignored.	AFS/HFT

Mode of determination of market value of investments(AFS and HFT categories)

Security Type	Mode of determination
Central Govt. securities	At market price as per quotations put out by FIMMDA.
State Govt. securities and securities guaranteed by central/state Govt., PSU bonds not being advances	On appropriate yield to maturity (YTM) as per FIMMDA guidelines
Treasury bills, Commercial papers, Investments in sponsored Regional Rural banks	At carrying cost
Equity shares	At market price, if quoted, otherwise at break-up value of the share as per latest balance sheet (not more than 1 year old), otherwise at Re.1 per company
Preference shares and Debentures (not in the nature of advances)	At market price, if quoted, or on appropriate YTM not exceeding redemption value as per FIMMDA guidelines
Mutual funds	As per stock exchange quotation, if quoted, or at repurchase price/NAV.
Investments in subsidiaries, joint ventures and other investments	At carrying cost less diminution.
Profit evaluation of foreign currency transactions	At year end rates (Nostro mirror balances, monetary assets and liabilities, outstanding spot exchange contracts) and at forward rates for forward contracts classified tenor-wise --- rates and methodology prescribed by FEDAI
Hedge swaps	Interest rate swaps which hedges interest bearing asset or liability to be accounted for on accrual basis except the swap designated with an asset or liability that is carried at market value or lower of cost or market value.
Trading swaps	Are marked to market

Investment Fluctuation Reserve (IFR)

With a view to building up of adequate reserves, banks have been advised by RBI to build up IFR of a minimum 5% of the investment portfolio within a period of 5 years. IFR should be computed with reference to investments in HFT and AFS category. Banks should transfer maximum amount of the gains realized on sale of investment in securities to IFR.

Risk management As per the guidelines issued by RBI, banks encounter three types of major risks – Credit risk, market risk and the operational risk.

Credit Risk: Credit risk is the potential that bank bor-

rowers/ counter party fail to meet the obligations on agreed terms. Instruments and tools, through which credit risk management is carried are:

- *Exposure ceiling*: Prudential limits linked to the capital funds of the counter party.
- *Risk Rating Model*: Set up a comprehensive risk scoring system. Clearly define rating thresholds and review of the ratings periodically.
- *Portfolio management*: Quantitative ceiling on aggregate exposure on specific rating categories, distribution in various industry, business group, etc.

Market Risk: Market risk may be defined as the possibility of loss to bank caused by changes in market variables. It is the risk that movements in equity markets, interest rate, currency exchange rates and commodity prices will adversely affect the bank. Market risk management provides a comprehensive and dynamic framework for measuring, monitoring and managing liquidity, interest rates, foreign exchange that needs to be closely integrated with the bank's strategy.

The bank may lay down various ceiling limits borrower-wise, industry-wise, security type-wise in its investment policy. Banks should continuously monitor compliance with the laid down norms.

Evaluation of internal control: The existence of an effective system of internal control is a sine qua non for efficient treasury operations. It is important that operations of a treasury are effectively segregated among:

- Front office – Dealing in the financial markets for lending and borrowing funds, buying and selling in financial instruments.
- Back office – Settlement, delivery, accounting, custody and reconciliation
- Mid office – Risk monitoring and control.

An audit of Treasury includes an audit of all the three offices.

Amongst other things, the following procedures are to be clearly established:

- Functioning of treasury and the products dealt by it are clearly documented along with policies (risk/market/credit management, investment, asset liability management etc).
- Authority to put through deals are clearly specified;
- Dealings powers of each of the dealers are fixed and communicated to all
- All financial decisions and deviations from laid down procedures are required to be reported to the next higher level for confirmation/ information;
- Monitoring and controlling of all treasury activities are on a continuous/ online basis.
- A system of concurrent audit is required to be in place in treasury in terms of RBI guidelines.

Regulatory provisions

- Section 19 of the Banking Regulations Act, provides overall limits on the holding by banks in shares of companies. This extends to shares held as pledgee, mortagagee or as absolute owner.
- Circulars issued from time to time by RBI, FEDAI and FIMMDA. Frequent reference to their web sites would be helpful. References to some of the extant master RBI circulars are furnished below: -
  - Prudential norms on income recognition, asset classification, provisioning and other related matters dated 2.12.2004
  - Prudential norms for classification, valuation and operation of investments portfolio by banks dated 17.7.2004
  - Maintenance of statutory reserves Cash Reserve Ratio (CRR) and Statutory Liquid Ratio (SLR) dated 26.8.2004
  - Guidelines for issue of Certificate of deposits dated 12.7.2004
  - Risk management and Interbank dealings dated 1.7.2004
  - Guidelines for issue of Commercial paper dated 1.7.2004
  - Call/ Notice money market operations dated 3.7.2004
  - Export Credit in foreign currency dated 1.9.2004.

EDP controls (AAS 29): The extent of computerization is usually extensive in treasuries. This calls for strict controls in such an environment. Robust software covering the entire gamut of functionality required for smooth functioning of treasury, a proper security environment, controls in place to prevent unauthorized usage of files, systems, etc, start/end-of-the day process, business continuity and disaster recovery plans, well documented user and technical manuals, audit trails in the software, exception reports, complete trail of all back end changes made are a must. Computer assisted audit techniques and a tool, which could extract data to analyze them and identify exceptions, would be invaluable for review of EDP controls.

Audit programme: A suggested audit program for carrying out the audit is enclosed. This is to be modified or adapted to individual needs.

Long Form Audit Report

These are to broadly cover:

- Existence of investment policy
- Adherence to investment policy and compliance to RBI guidelines.
- System of purchase and sale of investments, delegation of powers, reporting systems, segregation of back office functions etc.
- Controls over investments including periodic verification/reconciliation of investments with book records
- Valuation mode, changes in valuations compared with previous year, adequacy of provisions
- System of monitoring income from investments.
- Software/system analysis
- SLR/CRR requirement-system of ensuring compliance
- Procedure for revaluation of Nostro accounts and outstanding foreign exchange contracts.
- Review of vostro accounts
- Reconciliation of FCNR, EEFC and RFC balances and monitoring deployment of funds.
- Claims arising out of delayed settlement of Interbank funds
- Borrowings outside India

Illustrative checklist for Bank Treasury Audit

Particulars	Com-ments	Working paper ref.
Salient observations of concurrent auditors, RBI etc. and follow up action taken		
Whether there is a functional separation of trading, settlement, monitoring, control and accounting?		
Whether there is a clear bifurcation of transactions of own investments and PMS?		
Whether the limit for the dealer and authority to put through transactions been followed?		
Whether deal slip is prepared for every transaction entered?		
Whether deal tickets are serially numbered and are there adequate controls with regard to unauthorized/unaccounted use of the deal tickets?		
Do the deal ticket give all the required particulars including the time of the deal and are these checked / signed / initialed by the dealer		
Ensure that alterations and cancellations on deal slips are authorized by the Treasury Manager		
Check that the copy sent to the counter-party is signed by the client and deals are supported by confirmation letter from the counter party		
Does the bank have an approved panel of brokers separately for capital market, wholesale debt segment, forex?		
Whether the deals done through brokers are only with the approved ones?		
To be ensured that the role of the broker is restricted to that of bringing the two parties to the deal together.		
Brokerage paid is at the approved rates and TDS is deducted as per the provisions of the Income tax Act, 1961.		
It should be ensured that all transactions made by the bank are in accordance with the approved investment policy and RBI regulation		
Credit Risk To check whether the counter party exposure limits have been separately specified for all transactions? To check for the excesses and to be ensured that they are ratified by the competent authority.		
Market Risk Check for various limits specified in the investment policy. To check for the excesses and to be ensured that they are ratified by the competent authority.		
Interface between front and back offices Is there seamless interface between the front and back offices? In other words, how are deals put through by front office captured by back office and what is the system of reconciliation between the two		
MONEY MARKET Are there any over-sold positions?		
To be ensured that rates at which the deals are done are in line with market rates.		

Particulars	Com-ments	Working paper ref.
Identify a sample of purchase and sale of investments and vouch them keeping in mind internal procedures, RBI regulations, authorization powers, counter party contracts, price feeds etc.		
Whether all investments are appropriate categorized at the time of acquisition?		
Whether capitalization of charges is as per the internal policy? To be ensured that charges to be considered as revenue is not capitalized.		
Whether any shifting of securities is effected? Are they in accordance with the RBI guidelines? Is the loss at the time of shifting provided?		
Ensure that broken period interest paid to seller is not capitalized as a part of cost but treated as expense		
Check for the accuracy and completeness of: ❖ Book value of securities in the portfolio; ❖ Interest accrual in case of dated Govt./debt securities; ❖ Amortization in case of securities held under HTM category; ❖ Income/dividends accounted in case of discounted instruments/shares/mutual funds. ❖ Profit/ loss calculation on sale ❖ Valuation as per norms		
Ensure whether classification of NPA and their accounting is as per statutory regulations		
Half yearly review of the investment portfolio undertaken by the bank and whether the same is forwarded to RBI within the stipulated time?		
Examination of reconciliation: ❖ Confirmation to be obtained from the Public Debt Office of RBI for securities (SGL & CSGL), custodian or depository organization (including rights, bonus), and to be crosschecked with bank's books. ❖ Scrips held in physical form to be physically verified ❖ Reconciliation in the balance of securities as per front and back office records.		

Particulars	Com-ments	Working paper ref.
FOREX Are there separate dealers for Interbank deals and customer / merchant trade deals?		
Whether any limits are fixed for transactions to be reported by 'B' category (foreign exchange designated) branches and if so, whether they are reported promptly for taking into position? i.e., the bank is not running any uncovered position in respect of transactions undertaken by the branches?		
Is the bank submitting consolidated position sheets to the higher authorities?		
NOSTRO Accounts: Reconciliation and balance confirmation of nostro accounts to be checked. Age-wise analysis of outstanding entries with reasons to be obtained from the bank		
Forex Suspense / Inter branch account: Age-wise analysis of outstanding entries in Forex Suspense / Inter branch account to be done. Has provision for old debit items been made as per extant RBI guidelines?		
FOREX PROFITS/LOSSES ❖ Ensure that the bank reckons the Nostro balances as per Mirror Accounts and the outstanding forward transactions as at the date of revaluation for adjustment of the profits / losses? ❖ Analyze the reasons for increase/ decrease in profit. Analysis to be separately done for Interbank and merchant transactions? ❖ Whether there are any differences between the profit evaluated as per the back office and the front office.		
Merchant related contracts Whether the merchant related contracts (bills, PCFC, forward contracts, etc.) shown as outstanding/ overdue in treasury records matched with branch records, particularly overdue items.		

Particulars	Com-ments	Working paper ref.
Limits: Are the following adhered to? ❖ Counter-party exposure, daylight, overnight limits ❖ Stop loss limit? ❖ Dealing limits? ❖ Aggregate Gap Limit (AGL)/ Individual Gap Limits (IGL) ❖ Value at risk Whether all limits breached been explained and ratified?		
Swap Deals: ❖ Is any swap deal undertaken at level rate (i.e., rate of both the leg of transaction is the same) and if so, whether is it properly explained. ❖ In case of swap deals, do the spot rate and the swap differences give a realistic reflection of the prevailing conditions in the inter-bank market? ❖ Whether swap deals were for trading in forward and/ or covering merchant positions?		
Does the bank prepare Daily Rate Scan Report for submission to an official independent of the dealing department?		
Whether there is a proper procedure for hedging against possible exchange losses in respect of foreign exchange transactions?		
DERIVATIVES		
Whether interest rate swaps were undertaken only with scheduled banks (other than RRB), Primary Dealers (PD), All India Financial Institutions (FI) and corporates?		
Has the bank used ISDA documentation for executing IRS/FRA		
Whether the transactions for hedging and market making purposes recorded separately		
Whether the transactions for market making purposes marked to market and accounting entries passed ?. Whether MTM is in accordance with the RBI guidelines.		
Whether the bank has adhered to the Capital Adequacy Norms applicable		

Particulars	Com-ments	Working paper ref.
Has the bank ensured that the corporate counter parties are undertaking IRS/FRA only for hedging their own rupee Balance Sheet exposures		
Whether the exchange of payments made at frequent interval is independently checked by back office.		
Whether accrual entries passed in the books are accurate.		
Whether Option premium received/ paid is dealt in accordance with the guidance note issued by ICAI.		
Maintenance of SLR and CRR		
Verify position of SLR and CRR on select dates and ensure adherence to the same ● Correctness of the compilation of DTL positions ● Maintenance of liquid assets. ● For determining the DTL position, weekly trial balances as on Friday received from different branches are consolidated at the head office. The central auditor should request the branch auditors to verify the correctness of the trial balances and cash balance at the branch on selected dates. As regards weekly returns received from unaudited branches, the return should be broadly reviewed on a sample basis to identify any prima-facie errors/ inconsistencies.		
Borrowing and Lending ● To identify select transactions and verify them ● To verify whether rates of interest are in line range of rates specified in RBI website ● Year end balances are confirmed ● Interest payable/receivable if any are provided/taken credit. ● Borrowings and lending in foreign currency are translated at year-end rates. Are in accordance with internal/RBI prudential norms.		
Disclosures Whether all required disclosures made?		