Taking 'Bank Audit Challenge' in Stride

It needs no reiteration that Banking is the backbone of today's economies, helping channelise idle capital to fruitful economic activity. As such, it is also an important tool in the hands of our Government to prioritise socio-economic development through allocation of precious finance to and for implementation of its ambitious schemes through priority sector lending policies, agricultural loans, MGNREGA disbursements, subsidy disbursements, etc. The European sovereign debt crisis and the US sub-prime lending crisis and the resultant collapse of "Too Big To Fail" banks, underlined how the contemporary banking industry is also crucial to the political stability of the countries.

In the backdrop of the global economic slowdown that has gripped the world economy, world over, the banking industry is witnessing declining asset quality across borrowers, implying declining profitability and risk of capital erosion, stricter lending norms on account of downgrading of borrowers, particularly, small borrowers, higher lending rates on account of enhanced default risk, ... and the circle continues.

For the bank auditors too, these are challenging times. Be it the Government, the regulators, the society, anyone and everyone, the expectation is for the auditors to not only perform well in their conventional role of lending credibility to the financial statements but also help strengthen the governance practices in the banking industry. The challenge for the Profession lies in seamlessly integrating these expectations in their role as statutory auditors.

In the above background, auditors' commitment to audit quality and their close coordination with those charged with governance in the banks, particularly, audit committees has assumed added importance. Standards on Auditing (SAs) are a pre-requisite to ensure audit quality. Obtaining adequate understanding about the risks present in the banking system as well as in the internal and external environments in which a bank operates is essential. These risks could arise out of a number of factors including new technology, new business models, overseas operations, new accounting and other legal/regulatory requirements, etc. As a corollary, auditor's understanding of the bank's systems and processes in place to identify and address those risks would help the auditors to focus on critical areas, design appropriate audit procedures, decide optimum time and resource allocation, timely execution of work and avoid any last minute surprises.

Compliance with the Standards on Auditing not only helps ensure quality in audits, it also helps audits transform from a mere statutory compliance into a real value-add function. In fact, they can help build a stronger symbiotic between the statutory auditors and audit committees and contribute to effective governance. For example, the information generated during the risk assessments and internal control evaluations carried out by the statutory auditors can be of use to the Audit Committees in discharging their responsibilities relating to review of risks facing the entity, including financial statement risks. The Guidance Note on Audit of Banks is another important publication that the statutory bank auditors, central as well as branch, need to follow.

Similarly, in addition, the other very important aspects from the perspective of the Audit Committees of banks include the 'statutory auditor's use of professional skepticism in, for example, whether management estimates reflect economic substance of the transaction and their consistency with the auditor's own knowledge of the bank's business' and 'completeness and accuracy of management's records and documents like those relating to the bank's lending activities'. The auditor procedures with respect to audit of disclosures such as compliance with Accounting Standards, overall presentation of financial statements, adequacy of disclosures in providing necessary information to the users and how the auditor deals with the disclosures not considered or appropriate have also special significance.

At this juncture, it may also be worthwhile to remember that true and fair view is a dynamic concept. Its content evolves in response to changes in, *inter alia*, accounting and business practice. It is inherent in the nature of the true and fair view concept that financial statements will not give a true and fair view unless the information they contain is sufficient in quantity and quality to satisfy the reasonable expectations of the readers to whom they are addressed and such expectations change over time.

Effective statutory audits and good governance in banks, therefore, are a collective responsibility/effort of the statutory auditors and those charged with governance in the banks, particularly, the audit committees. A regular and closer interaction between them can go a long way in ensuring that. While it would be fruitful if the statutory auditors engage in a dialogue with the Audit Committees at the various stages of their audit, beginning from planning and ending at reporting; it is also equally essential that the Audit Committees ensure that there is adequate opportunities and environment for the statutory auditors to have an uninhibited and frank discussion on crucial issues with the former.

-Editorial Board

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