OPEN BOOK EXAMINATION

NEW SYLLABUS

441

***Roll No.* ....**

Time allowed : 3 hours ***Maximum marks : 100***

Total number of questions : 6 ***Total number of printed pages : 7***

NOTE : *Answer* ***ALL*** *Questions.*

1. *Case Study* :

The accounting system followed by the banks in India, differs from the general accounting system followed by companies and other business entities. Nevertheless, all banks are required to prepare and present their Annual Financial Statements as per specified formats in compliance with the provisions of Banking Regulation Act (B.R. Act), the Companies Act, RBI directions and the ICAI Accounting Standards. Banking Companies are required to provide a statement of all the accounting policies followed in preparing these financial statements and also required to comply with disclosure/additional disclosure requirements as advised by Reserve Bank of India (RBI) from time to time relating to capital, lendings and others.

Like any other business entity banks also follow the mercantile system of accounting. However there is a slight difference in the methodology followed by banks when compared to other commercial entities. The reason of difference is that the banks are entering the transactions of customers first, in ledgers (which are subsidiary books under conventional accounting) rather than in Journals. This is so because, accounts of customers which are maintained in ledgers should be accurate and must be free from errors so that accuracy is being maintained as to the transactions.

Financial Statements of banking companies are an important source of information for a variety of stakeholders. These financial statements are prepared after an extensive compliance with the directions and guidelines issued by RBI and other regulatory authorities, and therefore, contain a treasure of useful information. One should necessarily focus on :

- Requirements regarding accounts and audit of banking companies.
- Features of accounting system of banks.
- Books of account of banks.
- Presentation and formats used for financial statements.
- Accounting treatment of various items.
- Disclosure requirements.

Sections 29 to 34A of the B.R. Act deal with the accounts and audit of banking companies. Section 29 of the B.R. Act casts a responsibility on every banking company incorporated/ operating in India which are involved in transacting the business of banking through its branches, prepare and submit Balance Sheet and Profit & Loss Account for the financial year in the specified formats set out in III-schedule of the Act as on the last working day of that financial year. Such Balance Sheet and P&L Account should be signed by the manager or the principal officer and at least by three directors, if there are more than three directors and if only three directors then all of them should sign the same. However, for a foreign bank operating in India, the manager or principal officer of the concerned bank should sign these statements. The central government has the powers to amend the formats of Balance Sheet and P&L Account as given in section 29 of B.R. Act and thereafter the banks are required to prepare the financial statements in these formats only.

According to section 30 of the B.R. Act, the Balance Sheet and P&L Account prepared are to be audited by a duly qualified person as per applicable law for the time being in force without prejudice to anything contained in the Companies Act or any other law for the time being in force. Where the Reserve Bank of India is of opinion that it is necessary in the public interest or in the interest of the banking company or its depositors so to do, it may at any time by order direct that a special audit of the banking company's accounts, for any such transaction or class of transactions or for such period or periods as may be specified in the order, shall be conducted by the same or by a different auditor. The RBI may either appoint a person duly qualified under any law for the time being in force to be an auditor of such banking company or direct the auditor of the banking company to conduct such special audit and the auditor shall comply with such directions and make a report of such audit to the Reserve Bank of India and forward a copy thereof to the banking company too.

As per section 31 of the B.R. Act, every banking company has to submit three copies of annual accounts consisting of Balance Sheet along with P&L Account prepared in accordance with section 29 of B.R. Act together with Auditor's Report to RBI within three months from the end of the period to which they relate. In the case of Regional Rural Banks (RRBs), they shall furnish the Balance Sheet and P&L Accounts to NABARD instead of RBI.

Under section 32 of the B.R. Act, a banking company (not other types of banking entities) has to submit three copies of Balance Sheet and P&L Account to the Registrar of Companies when it submits the same to RBI. Such banking company, also within a period of six months from the date of accounts and Auditors' Report, publish the same in a newspaper which is widely circulated where the banking company has its principal place of business. This compliance has to be done according to Banking Companies Regulation (Rules), 1949.

As per section 33 of the B.R. Act, in the case of foreign banks operating in India required to display a copy of audited accounts and Balance Sheet at a clear place in their notice board for public display. This has to be done before 1st Monday in the month of August every year.

Banks have to maintain a 'Regulatory Disclosure Section' on their website, where all the information relating to disclosures will be made available to the market participants.

Bank which have been listed on stock exchanges in India and abroad have to comply with terms of SEBI (LODR) Regulations, 2015 including reporting and other compliances regulations in a timely manner failing which they would be facing penal action including fines. Disclosures related to individual banks within the groups would not generally be required to be made by the parent bank.

In order to encourage market discipline, Reserve Bank of India has over the years developed a set of disclosure requirements, which allow the market participants to assess the key points of information on capital adequacy, risk exposure, risk assessment provisions and key business parameters to provide a consistent and understandable disclosure framework that enhances comparability. Banks are also required to comply with the Accounting Standard-1 (AS-1) on 'Disclosure of Accounting Policies' issued by the Institute of Chartered Accountants of India (ICAI). The enhanced disclosures have been achieved through the version of Balance Sheet and Profit & Loss Account of banks and enlarging the scope of disclosures to be made in 'Notes to Accounts'. As a standard practice to bring in uniform reporting 'Summary of Significant Accounting Policies' and 'Notes to Accounts' are to be shown in Schedule 17 and 18 by banks. RBI through its Master Circular No. : RBI/2015-16/99 DBR.BP.BC.No. 23/21.04.018/2015-16 dated July 1, 2015 has provided detailed guidelines in this regard.

In the backdrop of the above you are required to give answer to the following :

(*a*) Banks in India prepare their Annual Financial Statements as per specified formats. Explain where such formats have been prescribed for the banks to prepare their annual statement of accounts. Also explain the 'Act' which have a bearing on financial statements of banks ?

(*6 marks*)

(*b*) State the principal books of accounts which are being maintained by banks in India. In what respects the balance sheet of a bank is different from Balance Sheet of a company.

(*8 marks*)

(*c*) What are the particulars of Liabilities and Assets to be provided in the Balance Sheet of a Bank as being prescribed under the Banking Regulation Act ?

(*6 marks*)

(*d*) As a standard practice to bring in uniform reporting 'Summary of Significant Accounting Policies' and 'Notes to Accounts' are to be shown in Schedule 17 and 18 by banks. What are being required under major disclosure ? Also state the mandatory requirements of SEBI (LODR) Regulations 2015 which the banks have to comply relating to listing of securities on stock exchange.

(*8 marks*)

(*e*) (*i*) What are the items to be adjusted before disclosing Net Profit in the Profit and Loss Account of a bank ?

(*4 marks*)

(*ii*) Financial Statements of Banking Companies are an important source of information for a variety of stakeholders. Who are such stakeholders and why they need such statements ?

(*4 marks*)

(*iii*) Explain how the bank manages the economic risk due to fluctuations in the forex market.

(*4 marks*)

2. (*a*) State in brief the factors attributing to the increased importance of credit risk modelling in the banks.

(*4 marks*)

(*b*) Explain the various types of 'Market Risk' involved in banking business. Differentiate between 'Counter Party Risk' and 'Country Risk'.

(*8 marks*)

3. (*a*) A customer approached you as bank on 1st January, 2018 for sale to him :

(*i*) US Dollar 2,00,000 delivery on 31st March, 2018

(*ii*) US Dollar 1,00,000 delivery on 30th March, 2018

Assumptions to be taken as to Rate and Margin :

— Spot interbank 66.5000/5100

— Forward premia January 0.1350/0.1450

February 0.3050/0.3150

March 0.5500/0.5600

April 0.7700/0.7800

— Exchange margin @ 0.125%.

Calculate the rates to be quoted to the customer by the bank. Take last two digit in the multiples of 25.

(*6 marks*)

(*b*) Explain and narrate all those important factors having influence on forex markets movements more frequently.

(*6 marks*)

4. (*a*) What are the popular types of mortgages obtained by a banker ? How the mortgage(s) is/are enforced by the bank ? Cite the relevant provisions of the Banking Regulation Act or of Code of Civil Procedure as applicable.

(*6 marks*)

(*b*) Differentiate between 'pledge' and 'hypothecation' of goods as security. Which mode of security would a banker prefer ?

(*6 marks*)

5. (*a*) Explain the following terms with reference to 'Bonds' :

(*i*) Coupon rate

(*ii*) Yield to Maturity

(*iii*) Redemption value.

(*3 marks*)

(*b*) Based on the behaviour of the bond market, a set of theorems for bond valuation has been developed. State briefly these theorems used for the purpose of bond valuation.

(*9 marks*)

6. (*a*) Explain the following features of the Basel-III accord :

(*i*) Minimum Total Regulatory Capital Requirement

(*ii*) Counter Cyclical Buffer

(*iii*) Leverage Ratio.

(*6 marks*)

(*b*) 'Although a depositor is a creditor of the bank, but he is not a secured creditor'. Elucidate with reference to banker-customer relationship.

(*3 marks*)

(*c*) Explain the type of relationship between banks and their borrowing customers who borrow against securities from the bank.

(*3 marks*)

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