

437

DIRECTORATE OF COOPERATIVE AUDIT:ORISSA:DHUBANESWAR.

No.VI(1)62/99 2807 (P-VI)/Audit-8/Dated:- 11.5.2004

C I R C U L A R .

Sub:- Prudential norms for Income Recognition, Asset classification and provisioning thereof.

In order to reflect a Bank's actual & financial health in its Balance Sheet, prudential norms for income recognition asset classification and provisioning thereof has been fixed by the Reserve Bank of India/ NABARD which have been circulated by the B.C.S., Orissa and A.G.C.S., Orissa to Cooperative Banking institutions in the State under various circular covers for their strict implementation. It has been made clear in the said circulars that the income recognition should be based on record of recovery only and any unrealised income should not be taken to P/L account as income. If such un-realised income is taken to P/L account provision of equal amount has to be made like "Overdue Interest Reserve" on income generated on loan but not actually realised.

Of late it has come to notice that in case of cash credit, overdrafts and loan accounts where system of compounding interest is applicable as per schemes of finance, the Banks are debiting the Borrowers accounts by crediting the interest account the amount of interest generated on such loans. Therefore, even though such generated interest is not realised during the year, it is shown collected and added to loan balance of borrower. This is completely against letter and spirit of norm for income recognition and not reflective of correct financial position of the Bank in the Balance sheet.

In order to check this erroneous practice the following instructions are issued now.

1. Interest realised on any loan should be recognised strictly on the basis of record of recovery and not out of fresh/additional credit facility sanctioned to the borrower concerned, which is, otherwise, called paper transaction.

P.T.O.

2. Interest accrued in respect of performing assets may be taken to the same account as the interest reasonably expected to be received. But in such case when the accrued interest related to such borrowal account, is not actually received before the end of the year i.e 31st March or the account has to be treated as NPA before close of the year, such un-realised interest has to be reversed by debit to P/L account and credited to overdue interest Reserve Account/because this unrealised interest amount also become N.P.A. .

For example, if accrued interest is Rs.5000/- in respect of a performing advance of a borrower, the following entries can be passed in books of accounts.

(DR) Borrower's Account -Rs.5000/-

(CR) Interest Account -Rs.5000/-

If this accrued interest is not actually realised at the end of same accounting year, the amount of accrued interest is to be reversed by passing the following entries.

(Dr) P/L Account -Rs.5000/-

(Cr) Over Due Interest Reserve A/c -Rs.5000/-

While making provision, the amount held in overdue interest Reserve in performing loans and advances should be deducted from the aggregate loans and advances through reverse entry.

In case this accrued interest is realised subsequently, the following entries are to be passed.

(Dr) Overdue interest Reserve A/c -Rs.5000/-

(Cr) Interest Account -Rs.5000/-

3. Accrued interest in respect of non-performing assets (advances) is to be debited to interest Receivable Account and corresponding amount credited to overdue interest Reserve Account. For example, if interest accrued in respect of a cash credit loan of a borrower of N.P.A. account is Rs.5000/- the following accounting entries are to be passed.

(Dr) Interest Receivable Account -Rs.5000/-

(Cr) Overdue interest Reserve Account -Rs.5000/-

Subsequently if interest is actually realised, the following accounting entries are to be passed
 (Dr) Cash/Bank Account Rs.5000/-
 (Cr) Interest Account Rs.5000/-
 (Dr) Overdue Interest Reserve A/c Rs.5000/-
 (Cr) Interest Receivable A/c Rs.5000/-

The Banks are to show "Overdue Interest Reserve" on Liability side of Balance Sheet. Since the above account would contain overdue interest reserves in respect of both performing and non-performing loans and advances, it is advised to maintain separate ~~records~~ records in respect thereof to facilitate audit, inspection and management of the Bank to know the relative amounts.

This circular instruction shall have immediate effect. The financial statements of the Banks for 2003-2004 onwards should reflect the position in the above manner.

Memo No. 2808(36) / Dated: - 11.5.2004
 Auditor General of C.S., Orissa.

Copy forwarded to the Managing Director, O.S.C.B./OSCARD/Secretary of all C.C.Bs/Secretary of all U.C.Bs/Chief Executive, ~~Utkal~~ Utkal Coop. Banking Society Ltd., Bhubaneswar for information and necessary action.

Memo No. 2809 / Dated: - 11.5.2004
 Joint Auditor General of C.S. (O)

Copy forwarded to the Registrar of C.S., Orissa for information and necessary action.

Joint Auditor General of C.S. (O)

Memo No. 2810 (16) / Dated:- 11.5.2004

Copy forwarded to all Asst.A.G.C.S. of Circles for information and necessary action. They are requested to circulate the circular amongst the auditors of their circle for guidance.

Memo No. 2811 / Dated:- 11.5.2004 Joint Auditor General of C.S. (O).

Copy forwarded to the C.G.M., NABARD, Bhubaneswar for information.

Joint Auditor General of C.S. (O).

Memo No. 2812 (2) / Dated:- 11.5.2004

Copy forwarded to the D.G.M., R.B.I., Rural planning and credit Department, Bhubaneswar for /D.G.M., R.B.I., Urban Banks Deptt. Bhubaneswar for information.

Memo No. 2813 / Dated:- 11.5.2004 Joint Auditor General of C.S. (O).

Copy submitted to the Commissioner-Cum-Secretary to Government of Orissa Cooperation Deptt. for favour of kind information.

Joint Auditor General of C.S. (O)

Memo No. 2814 (40) / Dated:- 11.5.2004

Copy to All Auditors of Apex Coops including C.As/ G.F./Audit-I /30 Spare copies.

Joint Auditor General of C.S. (O)

Dash.5.5.2005.