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राष्ट्रीय कृषि और ग्रामीण विकास बैंक
NATIONAL BANK FOR AGRICULTURE AND RURAL DEVELOPMENT
उडीसा क्षेत्रीय कार्यालय/ ORISSA REGIONAL OFFICE
2/1 नयापल्ली सिविक सेंटर, पो.बा.सं - 179, भुवनेश्वर-751015
2/1 NAYAPALLI CIVIC CENTRE, P.B. NO. -179,
BHUBANESWAR -751015
टेलीफोन/Tel - 2557132/2557218(PBX) फैक्स/FAX :2552019
E-mail : nabbhu@sancharnet.in

नाबार्ड
NABARD

Ref No. NB (ORI) / DCRR.Cell / 7376 / DCRR-1/ 2010-11

22 December 2010

The Managing Director
Orissa State Coop.Bank Ltd.
Pt. J N Marg
Bhubaneswar

Important
Copy to all C...

Dear Sir

Implementation of Revival Package for STCCS -
Internal control system for PACS

As you are aware, in terms of the covenant No. 8(b)(iii) of the MoU executed by the State Governments with the GoI and NABARD for implementation of the GoI Revival Package for the Short Term Cooperative Credit Structure (STCCS), NABARD is required to design an **Internal Control system for PACS.** Consequent to the amendment of State Cooperative Societies Act to give effect to the reforms envisaged under the Package, PACS have now been given full autonomy in all financial and internal administrative matters.

2. Post reforms, PACS are expected to function as full fledged and self-controlled financial intermediaries that establish their own business policies to meet the challenges of a dynamic economic environment and business models. In order to enable the PACS to have fool proof systems and procedures, that would enable prudent decision making at their level, which would also help the higher financing agencies, regulators and other stakeholders to discharge their obligations smoothly and more responsibly, there is an urgent need to have a sound internal control systems in PACS. With the above objective, a detailed guidelines on the Internal Control System for PACS has been designed by NABARD and a copy of the same is enclosed.

3. The matter may be translated into local language and copy of the same may be sent to all the CCBs of the State with instruction to forward the same to all the PACS under their jurisdiction.. The DCCBs may also be advised to instruct the PACS to adopt the internal control system designed by NABARD.

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4. A copy of the English version of the guidelines is being endorsed by us to the DCCBs to avoid delay in the matter.

Yours faithfully

Sd/-

(P C Padhi)
Deputy General Manager

Encl : As above

Endt.No. NB (ORI) / DCRR.Cell / 7377 / DCRR-1/ 2010-11 of dated

Copy forwarded for information and necessary action to the :

1. Secretary, Cooperation, Govt.of Orissa, Orissa Secretariat, Bhubaneswar
2. Registrar of Cooperative Societies, Govt.of Orissa, Heads of Deptt.Building, Bhubaneswar with a request to suitably instruct all the DCCBs / DRCS / ARCS / AGCS in the matter.
3. Secretary, DCCB to take urgent necessary action and review the progess in DLIC and DLIC sub-committee meetings constituted vide Coop.Deptt,.GoO Order No.12608 dated 3.12.2010.
4. AGM(DD), NABARD with a request to review the progess in DLIC and DLIC sub-committee meetings constituted vide Coop.Deptt,.GoO Order No.12608 dated 3.12.2010.

(P C Padhi)
Deputy General Manager

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Encl : As above

Memo no. 1896 (16) Dtd. 22.3.2011.
VI(1) 13/2011 /Audit-8

Copy with copy of the guidelines on Internal control system for PACS formulated by NABARD forwarded to all AAGCS of circles for information and necessary action.

5 spare copies

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S.A.A.G.C.S. (Office)

INTERNAL CONTROL SYSTEM FOR PACS

BACKGROUND

In terms of the covenant No.8(b)(iii) of the MoU executed by the State Governments with the GoI and NABARD for implementation of the GoI Revival Package for the Short Term Cooperative Credit Structure, NABARD is required to design Internal Control system for PACS.

As per GoI Revival Package for strengthening of Short Term Cooperative Credit Structure, State Cooperative Societies Act have been amended by the implementing States to give effect to the reforms envisaged under the Package. Consequent to the amendments, PACS have been now given full autonomy in all financial and internal administrative matters. Post reforms, PACS are expected to function as full fledged and self controlled financial intermediaries that establish their own business policies to meet the challenges of a dynamic economic environment and business models. In order to enable the PACS to have fool proof systems and procedures, that would enable prudent decision making at their level, which would also help the higher financing agencies, regulators and other stakeholders to discharge their obligation smoothly and more responsibly, there is an urgent need to have a sound internal control system in PACS. With the above objective, an Internal Control System for PACS has been designed by NABARD.

INTERNAL CONTROL SYSTEM FOR PACS

I. INTRODUCTION

A system of effective internal control is a critical component of any organisation and foundation for the safe and sound operations of organisation. As the systems are means to achieve the objectives and translate the policies into action they have to be simple and efficient. Such systems should facilitate the employees of the organization to be efficient and effective and at the same time offer good scope for appropriate initiative.

Main objectives of internal control system are to ensure that :

a) business is conducted in an orderly, prudent manner in accordance with established policies,
b) transactions are entered into only under general or specific authority,
c) assets are safeguarded and liabilities controlled,
d) accounting and other records provide complete, accurate and timely information,
e) management is able to identify and assess the risk of the business.

II. Major elements of Internal Control

The system should provide measures for prevention of irregularities by evolving controls at different levels. The basic elements of any good control system are :

i)Division / segregation of work
ii)Delegation of specific responsibility/ authorisation
iii)Checks & counter checks
iv)Well-defined procedures.

Division of work

a)Work allotted should be specific & identifiable.
b)Role clarity of employees so as to make them accountable for performance of role assigned.

c)Division of work should be such that no employee shall have absolute control over the financial operations of important nature.

Delegation

a) In delegating the powers, the authority and responsibility of each employee should be clearly defined.
b)There should be a system of reporting, on a periodic basis, to the higher authorities.

Checks and counter checks

In-built checks and counterchecks as regards maintenance of books of account, custody of valuables, operations of bank accounts, etc.

Well-defined procedures

Book of Instructions/ Manual clearly indicating, step by step, the procedure to be adhered to for handling items of work relating to all important aspects of PACS functioning is required to be prepared, updated from time to time and followed.

III. Internal Control Measures(ICM)

The various internal control measures to be adopted by PACS are as under:

1.Risk assessment control

The PACS are generally exposed to the following types of risks:

a)Credit risk
b)Interest rate risk
c)Liquidity risk
d)Operational risk

By analysing the MIS statements prescribed by NABARD, it is possible for PACS to make various risk assessment. The Secretary of PACS should put up important MIS statements to Management Committee of PACS periodically. MIS will facilitate the PACS to function as full fledged and self controlled financial intermediaries

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with their own business policies to meet the growing demand of members.

2. Accounts control

Proper maintenance of accounts, ledgers and other registers is a must with daily ledger posting, verification of entries by officers from the vouchers, balancing of ledgers, reconciliation of entries in bank accounts periodically.

PACS are required to follow Common Accounting System(CAS) prescribed by NABARD by using Manual prepared by NABARD for implementation of CAS. For the sake of transparency,better maintenance of accounts and for presenting true and fair picture of the financial position of the societies, it is imperative that PACS prepare the financial statements in the formats prescribed in the CAS.

3. Administrative control

a) fixing staff accountability for irregularities and malpractices at all levels

b) framing guidelines for delegation of financial powers to different staff levels in respect of sanction of advances,documentation,post-sanctioning monitoring,etc.

4. Audit and inspection

Audit is an analysis of the operations of an organisation with correct and honest record keeping in accordance with sound accounting principles. The basic purpose is to assess the integrity of books of account and other records. The scope of inspection is broader than that of audit and is fundamentally a qualitative review of the affairs of an organisation.

PACS are audited by Govt. auditors or Chartered Accountants and inspected by CCB/other agencies. PACS are required to furnish compliance reports promptly for audit and inspection reports. PACS should rectify the defects pointed out in inspection & audit reports and also initiate necessary steps to ensure that defects pointed out during audit & inspections are not repeated in future.

5. House Keeping

Efficient functioning of PACS depend on the sound housekeeping functions.

The basic functions of house keeping require the following:

(a) Maintenance of books of accounts adequately and properly to meet the requirements of CAS.
(b) Such books should be maintained clean without any alterations,overwritings, etc.
(c) Independent checking and authentication of financial transactions.
(d) Balancing of books of account at periodical intervals
(e) PACS are required to attach more importance particularly for balancing of deposit,loan,sundry debtors and creditors ledgers periodically.
(f) Balancing Register should be checked by a responsible official/member of MC
(g) PACS should make proper security arrangements so that it is less vulnerable to dacoities and robberies
(h)PACS should ensure that assets of the PACS(cash,building/godown,jewellary,stocks etc.)are covered by insurance and it is renewed promptly

6.Cash & Bank balance
The following ICM are suggested

(i)Cash
(a)Maintenance of double cash scroll, separately by cashier and by Accountant/ Secretary.
(b)Joint custody of cash
(c)Surprise verification of cash by an official/member of MC unconnected with the custody thereof
(d)System of recording of cash after close of cash

(ii)Balances with banks
(a)Joint operation of accounts maintained with banks
(b)Periodic reconciliation of bank accounts
(c)Follow up of entries remaining unadjusted for a long period.

7.Custody of security items
The following ICM are suggested
(a)Blank cheque books/FDR forms should be under the custody of authorised officials and duly accounted for.
(b)Account opening forms, specimen signature cards, loose ledger sheets, etc. should also be kept under proper custody.

8. Advances

The following ICM are suggested

a)Delegation of adequate power to different levels of officials.

b)Mechanism for monitoring the powers exercised by officials under delegated power.

c)Maintenance of document register and proper custody of documents

d)Verification of documents periodically by officials /member of MC unconnected with the custody thereof

e)Receipt & scrutiny of stock statements

f)Periodic visit of units to verify the assets created

g)Periodic verification of stocks pledged to society

h)Periodic verification of golds pledged to society

i)Joint custody of gold pledged to society

9.Investments

The following ICM are suggested

a)Proper custody of investment scrips

b)System of periodic verification of scrips

c)Maintenance of investment register

d)Ensuring that interest/dividend on investment is received promptly

e)Ensuring that on maturity, investment amount, interest/dividend received promptly.

10.Suspense Account/Sundry debtors & Creditors A/C

There should be a practice of periodic balancing of the above accounts and taking timely action for adjusting the outstanding entries.

11. Non Credit business

Following ICM suggested

a)Periodic verification of stock of fertilizer,seeds,pesticides

b)Periodic verification of stock of PDS commodities

c)Periodic verification of stock of Non PDS consumer items

d)Periodic verification of stock of foodgrains and other commodities under procurement scheme.

e)Periodic verification of stock of materials under Mid day meals scheme

f)Periodic verification of other stocks/goods/work in progress

12. Returns

i. Periodic Returns

a) MIS statements prescribed by NABARD should be submitted promptly to higher agencies

b) PACS are required to compile the MIS statements by referring to Handbook on MIS prepared by NABARD

c) A sub Committee of Management Committee is required to analyse the statements periodically

d) A Return Register is required to be maintained to ensure timely submission of MIS and other returns

ii. Submission of returns to RCS and other agencies

PACS are required to submit a number of returns/statements to RCS/ DCCB and other agencies. Broadly, the returns/statements may be of two types:

a) Statutory returns
b) Other returns

Statutory returns are required to be furnished as per provisions of Cooperative Societies Act/other Acts and are mandatory for PACS to submit the same in the stipulated time frame.

13. Planning & budgeting

Each PACS may have its short term and long term goals. Broadly, long range plans cover a period of 3-5 years and may be further broken down on annual basis. Short term plans, also called budgets, cover a period of 1 year. Annual budgets are further broken up on a quarterly basis.

The effort should be to see that budgets are based on realistic assessment and at the same time challenge is built into them. Budgeting should be supplemented by action plans spelling out specifics of activities and strategies which would go into the achievement of the goal.

Performance review should be a rigorous exercise, comparing actuals with budgets, explaining variances and indicating further course of action.

Management Committee of the PACS may review the budgets/plans periodically.

14. Monitoring of Frauds

Frauds can cause serious financial damage. Frauds in PACS are generally perpetrated by flouting established systems and procedures. A fraud need to be followed-up and monitored. Police action, follow up with insurance companies as also internal inquiries need to be initiated so that the PACS recovers its funds along with interest and is not put to pecuniary loss. Staff found guilty should be punished as per law/service rules.

15. Internal Control in Computerised environment

While computerisation of banking operations leads to improvement in staff productivity, this is not without attendant risks. Operational risk may be the most important risk category attendant to the use of computers in the PACS. Operational risk arises from the potential for loss due to loss of important data, computer abuses/ frauds caused by outsiders or employees, improper protection of hardware and software, systems deficiencies, loss of integrity of information on account of unauthorised/ intentional change or manipulation of data, etc.

Therefore, PACS should have a proper audit/ control over such system. PACS should exercise necessary checks and controls which would minimise the risks involved. Major factors which lead to security violations in computers are the absence of security policies and measures, inadequate and incomplete system design, programming errors, inadequate logical access controls, absence of procedural controls, ineffective employee supervision and management controls.

A few measures that would be of help in this regard are

a) Appropriate control measures involving physical, logical and procedural should be devised and documented to protect the system from attacks of unscrupulous elements within and outside the organisation.
b) Adoption of policy for upgrading skills and knowledge of staff in computer use and application.

c) Development of contingency plan to limit the risk of disruption in internal process or in service delivery. The plan may address data recovery, alternative data processing capabilities, emergency staffing, etc.

d) In order to ensure a consistent and reliable system for inputting, processing and generation of output data, the following checks should be in place.

i) test to identify erroneous processing
ii) test to assess the quality of data
iii) test to identify inconsistent data.
iv) Maintain back up of important documents and datas
iv) Appropriate arrangement for disaster management

16. Review by Sub-Committee of Management Committee(MC)

A sub-Committee of MC may be constituted to review the internal control system in the PACS and initiate measures to promote excellent house keeping, accounting system and maintain proper control over the PACS operations.

17. Rotation of duties

In addition to above 16 internal control measures, PACS with more than five staff may also effect periodical rotation of duties among staff

18. Branch Control

In addition to above 17 internal control measure, following measures may be adopted by PACS operating through branches.

i) Inter-branch Accounts and reconciliation thereof (applicable for PACS operating through branches)

Transactions between branches and between HO and branch is a natural consequence due to varying nature of business needs. Such transactions are called inter-branch transactions, and account in which these are reflected is called Inter-branch Account. Inter-branch account is a highly fraud-prone area. Pendency in inter -branch accounts in alarming proportion has become a major concern. Inter branch account should be reconciled periodically and take timely action for adjusting outstanding entries.

ii) Control over branches are normally exercised through the following methods:

a)Issue of Book of Instructions/ Manual/ Circulars indicating procedures with in-built checks and controls,
b)Prescription of periodic returns by the bank,
c)Inspection and Audit,
d)Visit of branches,

e)Branch Adjustment Accounts & reconciliation thereof.

iii. Visit to branches

There should be a system of branch visits at periodic intervals by Secretary /member of MC. Such visits have to be regular, planned and structured. The officer visiting the branch must carry a brief branch profile and the list of issues to be handled during the visit. Visits should not become rituals. Visits are supplements to internal audit/ inspection, not substitutes. For the visits to be purposeful, there should be visit reports. The major findings of the reports should be placed before the Board of the bank at periodic intervals. Visits have to be used to tone up the system and also to send warning signals of any imminent problem or danger.

IV. ICS –Statements

PACS may prepare the following statements on quarterly basis and put up the same to MC so as to ensure that some of the essential internal control measures are put into practice in the Society.

ICS-1-Books of Account.

ICS-2-Balancing & Reconciliation

ICS-1-Books of Account-position for the quarter ending-

Name of PACS:

S.No	Item of work	Posting Completed upto	Checking Completed upto	Tallying Completed upto	Reasons for arrears, if any
1	**Day Book**				
2	**General Ledger**				
3	**Deposit Accounts**				
I	Saving Bank Account				
ii	Fixed Deposits				
iii	Recurring Deposits				
iv	Others				
4	**Loan Accounts**				
i.	ST(SAO) Loans / KCC Loans				
ii.	Medium Term / Long Term Agricultural Loans				
iii.	MT Conversion Loans				
iv.	MT / LT Reschedulement				
v.	Loans against pledge of agricultural produce				
vi.	SHG Loans				
vii.	Non-Farm Sector Lonas				
viii.	Loans against Deposit				
ix.	Loans for Consumer Durables				
x.	Gold Loans				
xi.	Loans to Staff Members				
xii.	Other Loans (to be specified)				
5	**Stock Registers**				
I	Fertilizer				
ii	Seeds				
iii	Pesticides				
iv	PDS Commodities				
v	Non-PDS Consumer items				
vi	Food grains and other commodities under Procurement Scheme				
vii	Materials under Mid-day Meals Scheme				
viii	Other stocks / goods /Work in progress				
6	**Sundry Debtors Register**				
7	**Sundry Creditors Register**				
8	**DCB Register**				

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ICS-2-Balancing &Reconciliation-Position for the quarter ending-

Name of PACS:

Sl.No.	Particulars	Reconciliation/balancing done upto	Reasons, if there is arrears.
	Bank Reconciliation		
1	Name of bank-A/C.No.		
2	-do-		
3	-do-		
	Balancing of books		
4	Deposit ledgers		
A	Savings		
B	Fixed deposits		
C	---		
D	----		
5	Loan ledger		
A	ST-Agri.		
B	MT/LT-Agri.		
C	NFS(specify)		
D	Others(specify)		
6	Sundry Debtors		
7	Sundry Creditors		
8	Suspense A/C		