DegreeLive

Bachelor of Business Administration (BBA) | Fifth Semester | UK5DSCMGT302

Basics of Financial Accounting

Course Code: UK5DSCMGT302 • Module 3 Notes

degreelive.in

Module 3: Cash Book and Banking Transactions

Basics of Financial Accounting • Course Code: UK5DSCMGT302

Chapter 1: The Cash Book: Dual Character and Operational Structure

1.1 Meaning, Features, and Dual Identity of the Cash Book

The **Cash Book** is a specialized, chronological book of original entry designed to record all receipts and disbursements of cash and banking funds. In commercial enterprises, cash transactions—including cash sales, customer collections, cash purchases, supplier settlements, utility payments, and payroll disbursements—occur with greater frequency than any other transaction category. Consequently, maintaining a dedicated Cash Book is universally indispensable across small sole proprietorships, partnership firms, and multinational corporations alike.

The Cash Book occupies a unique, hybrid status in double-entry bookkeeping: it functions simultaneously as a **Book of Original Entry (Subsidiary Journal)** and as the **Principal Ledger Account (Cash and Bank Account)**:

- *As a Book of Original Entry:* Transactions involving physical cash or bank transfers are entered directly into the Cash Book at the moment they occur, supported by source documents (cash receipts, paying-in slips, cheque counterfoils, bank debit advices). Transactions recorded in the Cash Book are never entered in the general journal.
- *As a Ledger Account:* The Cash Book is structured exactly like a ledger account, featuring a Debit side (Receipts) and a Credit side (Payments). Because all cash and bank receipts and disbursements are permanently posted and balanced within the Cash Book itself, there is zero necessity to open a separate "Cash Account" or "Bank Account" in the general ledger. The Cash Book replaces them completely.

Core Structural Features of the Cash Book:

- *Strict Cash/Bank Scope:* Only transactions involving actual movements of currency or commercial bank balances are recorded. Pure credit purchases, credit sales, bad debt write-offs, or barter exchanges are completely excluded.
- *Receipts on Debit, Payments on Credit:* Following the Golden Rule of Real Accounts (Debit what comes in, Credit what goes out), all incoming funds are debited on the left-hand Receipts side, while all outgoing disbursements are credited on the right-hand Payments side.
- *Perpetual Positive Balance:* Because an enterprise cannot physically spend more paper currency than it possesses in hand, the Cash column of a Cash Book must always exhibit either a **Debit Balance** (cash on hand) or a **Zero Balance**. A credit balance in the Cash column is physically impossible. However, the Bank column may exhibit a **Credit Balance** if the enterprise holds an authorized Bank Overdraft facility.

Chapter 2: Typologies of Cash Books and the Triple Column Format

2.1 Classification of Cash Books

Depending on enterprise requirements and the complexity of banking arrangements, Cash Books are maintained in four standard formats:

1. Single Column Cash Book (Simple Cash Book): Designed for micro-enterprises that execute transactions exclusively in cash with zero banking or cash discount interactions. Features a single monetary amount column on each side (Debit for Cash Receipts, Credit for Cash Payments).

2. Double Column Cash Book (Two-Column Cash Book): Designed for growing firms. Features two monetary columns on each side. The two columns may be configured as:

- *Cash and Discount Columns:* One column for Cash and one column for Cash Discount (Discount Allowed on Debit side, Discount Received on Credit side).
- *Cash and Bank Columns:* One column for physical Cash and one column for commercial Bank account movements, tracking cheques and electronic fund transfers (NEFT/RTGS/IMPS).

3. Three Column Cash Book (Triple Column Cash Book): The comprehensive standard format used by commercial trading firms. Features three dedicated monetary columns on both the Debit and Credit sides: **Cash, Bank, and Discount**.

DegreeLive

RECEIPTS (Dr.) SIDE						PAYMENTS (Cr.) SIDE					
Date	**Particulars**	**L.F.**	**Disc**	**Cash**	**Bank**	**Date**	**Particulars**	**L.F.**	**Disc**	**Cash**	**Bank**
Date	To [Account]	*Folio*	*Rs*	*Rs*	*Rs*	*Date*	By [Account]	*Folio*	*Rs*	*Rs*	*Rs*

2.2 The Phenomenon of Contra Entries

A **Contra Entry** (derived from the Latin *contra*, meaning "against" or "opposite") is an accounting transaction that affects both the Cash Account and the Bank Account simultaneously within the Cash Book, requiring an entry on both the Debit and Credit sides. Because both sides of the transaction are completely recorded inside the Cash Book itself, no posting is required to any account in the general ledger. To flag this to auditors and prevent duplicate ledger postings, the letter **"(C)"** is entered in the Ledger Folio (L.F.) column on both sides.

Contra entries occur under two standard commercial circumstances:

- **1. Depositing Physical Cash into the Commercial Bank Account:** Cash is transferred from the office safe into the bank. In the Cash Book: Debit the **Bank Column** on the Receipts side (*"To Cash A/c"*, L.F. = C), and Credit the **Cash Column** on the Payments side (*"By Bank A/c"*, L.F. = C).
- **2. Withdrawing Cash from the Bank for Office / Business Use:** Funds are withdrawn from the bank account to replenish the office cash register. In the Cash Book: Debit the **Cash Column** on the Receipts side (*"To Bank A/c"*, L.F. = C), and Credit the **Bank Column** on the Payments side (*"By Cash A/c"*, L.F. = C).
- *Crucial Distinction:* If cash is withdrawn from the bank by the proprietor for **personal domestic use**, it is NOT a contra entry. It is a drawing: Credit Bank Column (*"By Drawings A/c"*), and post to the Drawings Account in the ledger.

2.3 Treatment of Cash Discount versus Trade Discount

Bookkeeping draws a rigorous conceptual and procedural line between Trade Discounts and Cash Discounts:

Comparative Dimension	Trade Discount	Cash Discount
Core Purpose	Granted by wholesalers/manufacturers to retailers to encourage bulk buying and allow retailers to earn retail trade margins.	Offered by creditors/sellers to debtors to incentivize prompt, early payment before credit expiration.
Timing of Deduction	Deducted directly from the gross catalogue list price on the face of the commercial invoice at the time of purchase/sale.	Calculated and allowed only at the time of final debt settlement if payment occurs within the cash discount window.
Ledger Accounting Entry	**NEVER recorded in any ledger account.** Purchases and sales are recorded strictly at net invoice price.	**Mandatorily recorded in books.** Recorded in the Discount columns of the Cash Book and posted to ledger accounts.
Account Nature	Zero accounting status.	Nominal Account. *Discount Allowed* is an operational loss (Dr.); *Discount Received* is an operating gain (Cr.).

Balancing the Discount Columns: A critical procedural rule: unlike the Cash and Bank columns, the Discount columns in a Three Column Cash Book are **NEVER balanced**! The total of the Discount Allowed column on the debit side is totaled and posted as a debit to the *Discount Allowed Account* in the ledger. The total of the Discount Received column on the credit side is totaled and posted as a credit to the *Discount Received Account* in the ledger.

2.4 Comprehensive Practical Problem: Three Column Cash Book

To demonstrate the operational maintenance of a Three Column Cash Book with contra entries, trade discounts, and cash discounts, consider the following transactions of Royal Merchant Enterprises during June 2024:

- June 1: Opening cash in hand Rs 25,000 and bank balance at SBI Rs 1,80,000.
- June 4: Sold goods for cash Rs 35,000.
- June 7: Purchased goods for cash Rs 18,000 and paid by cheque Rs 22,000.

DegreeLive

- June 11: Received a cheque from debtor Mahesh for Rs 28,500 in full settlement of his account of Rs 30,000 (discount allowed Rs 1,500). Cheque deposited into bank the same day.
- June 15: Cash deposited into SBI bank account Rs 20,000 (Contra Entry).
- June 18: Paid creditor Rajesh by cheque Rs 19,200, receiving a cash discount of Rs 800.
- June 22: Withdrew cash from bank for office petty cash use Rs 10,000 (Contra Entry).
- June 25: Withdrew cash from bank for domestic personal household use Rs 8,000.
- June 28: Mahesh's cheque deposited on June 11 was returned dishonoured by the bank. Bank debited bank charges Rs 100.
- June 30: Paid office staff salaries by bank transfer Rs 25,000.

RECEIPTS (Dr.) SIDE						PAYMENTS (Cr.) SIDE					
Date	**Particulars**	**L.F.**	**Disc**	**Cash**	**Bank**	**Date**	**Particulars**	**L.F.**	**Disc**	**Cash**	**Bank**
Jun 1	To Balance b/d	-	-	25,000	1,80,000	Jun 7	By Purchases A/c	-	-	18,000	-
Jun 4	To Sales A/c	-	-	35,000	-	Jun 7	By Purchases A/c	-	-	-	22,000
Jun 11	To Mahesh A/c	-	1,500	-	28,500	Jun 15	By Bank A/c (C)	C	-	20,000	-
Jun 15	To Cash A/c (C)	C	-	-	20,000	Jun 18	By Rajesh A/c	-	800	-	19,200
Jun 22	To Bank A/c (C)	C	-	10,000	-	Jun 22	By Cash A/c (C)	C	-	-	10,000
						Jun 25	By Drawings A/c	-	-	-	8,000
						Jun 28	By Mahesh (dishonour)	-	-	-	28,500
						Jun 28	By Bank Charges A/c	-	-	-	100
						Jun 30	By Salaries A/c	-	-	-	25,000
						Jun 30	By Balance c/d	-	-	32,000	1,15,700
Total	-	-	**1,500**	**70,000**	**2,28,500**	**Total**	-	-	**800**	**70,000**	**2,28,500**

Month-End Cash Book Audit Findings:
1. **Cash in Hand Balance:** Rs 32,000 debit balance carried down to July 1.
2. **Bank Balance at SBI:** Rs 1,15,700 debit balance carried down to July 1.
3. **Discount Columns:** Discount Allowed of Rs 1,500 is posted as a debit to *Discount Allowed A/c*; Discount Received of Rs 800 is posted as a credit to *Discount Received A/c* in the general ledger. They are not balanced against each other.

4.2 Practical Preparation of a Bank Reconciliation Statement (BRS)

To demonstrate the reconciliation of Cash Book and Pass Book balances, consider the position of Royal Merchant Enterprises on June 30, 2024. The Cash Book indicates a debit bank balance of Rs 1,15,700. On comparing with the SBI Bank Statement, the accountant discovers the following discrepancies:

- 1. Cheques totaling Rs 35,000 were issued to suppliers on June 28, but only Rs 20,000 was presented for payment before June 30 (Rs 15,000 unpresented cheques).
- 2. Cheques totaling Rs 25,000 were deposited into the bank on June 29, but were credited by the bank only on July 2 (Rs 25,000 uncredited cheques).
- 3. A customer directly deposited Rs 12,000 into the bank account via NEFT on June 29, which was not recorded in the Cash Book.
- 4. Bank credited interest on fixed deposit Rs 2,400 directly in the Pass Book without advice.

Degreelive

- 5. Direct debit for annual fire insurance premium Rs 6,000 paid by the bank under standing instruction, not recorded in the Cash Book.

Particulars	Amount (Rs)
Bank Balance as per Cash Book (Debit / Favourable)	**1,15,700**
Add:	
1. Cheques issued but not yet presented for payment (Rs 35,000 - Rs 20,000)	15,000
2. Direct deposit by customer into bank account via NEFT	12,000
3. Interest on fixed deposit credited by bank directly in Pass Book	2,400
Sub-Total Additions	**+ 29,400**
Total	**1,45,100**
Less:	
1. Cheques deposited into bank but not yet cleared/credited by bank	(25,000)
2. Insurance premium paid directly by bank under standing instructions	(6,000)
Sub-Total Deductions	**- 31,000**
Bank Balance as per Bank Pass Book (Credit / Favourable)	**Rs 1,14,100**

2.5 Point-of-Sale (POS) and Electronic Cash Drawer Synchronization

In contemporary retail environments (supermarkets, department stores, restaurant franchises), manual cash books are replaced by computerized Point-of-Sale (POS) systems integrated with barcode scanners, digital weigh scales, electronic payment card swipe terminals, and automated cash drawers. At the end of every operating shift, the POS system executes an automated **Z-Report (End-of-Day Settlement)**:

- *Cash Sales Reconciliation:* The Z-Report aggregates all scanned cash transactions. The store manager performs a physical cash drawer count (cash float + cash takings). Any discrepancy between the physical currency count and the POS report is immediately recorded as *Cash Short and Over*.
- *Card and UPI Reconciliation:* The POS system reconciles electronic payments against card terminal settlement batches, verifying that digital credit card slips match merchant acquiring bank clearing files.
- *Automated Accounting Interface:* The verified daily settlement data automatically posts as a consolidated compound journal entry into the ERP general ledger: debiting Cash in Hand, debiting Bank (for card/UPI receivables), and crediting Sales Account and Output GST accounts, ensuring zero manual transcription delay.

Chapter 3: The Petty Cash Book and the Imprest System

3.1 Operational Rationale and the Imprest System

In every operating commercial business, dozens of petty, minor operational expenditures occur daily—such as purchasing tea/coffee for visitors, postage stamps, courier envelopes, auto-rickshaw fares for office peons, bus tickets, cleaning soap, and stationery sundries. If the chief cashier were required to write formal bank cheques or record every Rs 20 or Rs 50 expenditure in the main Cash Book, the main cashier would be overwhelmed, and the Cash Book would become hopelessly cluttered.

To ensure administrative efficiency and tight internal control, enterprises establish a **Petty Cash System** managed by a junior employee designated as the **Petty Cashier**. The system operates on the universally acclaimed **Imprest System** (from the Italian *imprestare*, meaning "to advance"):

1. **Initial Imprest Advance:** At the start of an operating period (e.g., month), the chief cashier hands the petty cashier a fixed, predetermined round sum of cash termed the *Imprest Advance* (e.g., Rs 10,000). The petty cashier signs an acknowledgment receipt.

DegreeLive

2. **Disbursement against Vouchers:** Throughout the month, the petty cashier disburses small cash sums strictly against authorized, numbered **Petty Cash Vouchers** signed by the recipient and approved by department heads, attaching bus tickets, courier slips, or postage receipts.
3. **Recording in Analytical Register:** The petty cashier records each disbursement in an **Analytical Petty Cash Book**, classifying each payment into standardized thematic expense columns (Postage, Conveyance, Printing & Stationery, Office Tea/Refreshments, Sundry Expenses).
4. **Reconciliation and Reimbursement:** At the close of the month, the petty cashier totals the expense columns, presents the analytical book and original physical vouchers to the chief cashier for audit verification. Upon approving expenditures totaling, for example, Rs 8,450, the chief cashier issues a replenishment cheque or cash for **exactly Rs 8,450** (the exact sum expended).
5. **Restoration of Imprest Balance:** This reimbursement restores the petty cashier's cash float back to the exact initial imprest figure of Rs 10,000 at the start of the new month.

Core Operational Advantages of the Imprest System:

- *Fraud Prevention:* The petty cashier never holds more than the fixed imprest limit, strictly capping potential losses from embezzlement or theft.
- *Chief Cashier Relief:* Relieves the chief financial controller from petty interruptions, allowing focus on strategic cash management and treasury investments.
- *Automated Internal Audit:* The monthly replenishment review acts as a continuous, mandatory internal audit of all operational disbursements before funds are released.

3.2 Comprehensive Analytical Petty Cash Book Format

An Analytical Petty Cash Book features analytical expenditure columns that distribute expenses horizontally across departments, as demonstrated below:

Receipts (Rs)	Date	V.N.	Particulars	Total Paid	Postage	Conveyance	Stationery	Refreshments	Sundries
10,000	2024 May 1	-	To Cash (Imprest Advance)	-	-	-	-	-	-
-	May 3	1	By Courier Charges	350	350	-	-	-	-
-	May 6	2	By Auto fare for Peon	220	-	220	-	-	-
-	May 10	3	By Xerox and Printing paper	650	-	-	650	-	-
-	May 15	4	By Client Tea and Coffee	480	-	-	-	480	-
-	May 20	5	By Registered Speed Post	280	280	-	-	-	-
-	May 25	6	By Taxi fare for Auditor	850	-	850	-	-	-
-	May 28	7	By Office Dusting Brooms	180	-	-	-	-	180
-	**May 31**	-	**Total Monthly Expenditure**	**3,010**	**630**	**1,070**	**650**	**480**	**180**

DegreeLive

Receipts (Rs)	Date	V.N.	Particulars	Total Paid	Postage	Conveyance	Stationery	Refreshments	Sundries
-	May 31	-	By Balance c/d (Cash in hand)	6,990	-	-	-	-	-
10,000	May 31	-	**Total Balanced Float**	**10,000**	-	-	-	-	-

Imprest Replenishment Cycle: On June 1, the chief cashier audits the vouchers, inspects the physical cash balance of Rs 6,990 remaining in the petty cash tin, and issues an exact reimbursement cheque of **Rs 3,010**, restoring the operating float to Rs 10,000 for June.

3.3 Standard Format of a Petty Cash Voucher (PCV)

Every petty cash disbursement must be backed by an approved physical or electronic voucher containing verifiable audit metadata:

BHARAT COMMERCIAL ENTERPRISES — PETTY CASH VOUCHER			
Voucher No: PCV-2024-042	**Date:** 15-May-2024	**Account Head:** Conveyance	**Amount:** Rs 350.00
Paid To: Shri Ramesh (Courier Messenger) **Particulars:** Auto-rickshaw fare to deliver emergency legal contract documents to High Court premises. **Supporting Document:** Physical Auto receipt and digital GPS trip receipt attached.			
Prepared By: Petty Cashier	**Verified By:** Office Supervisor	**Approved By:** Accounts Officer	**Receiver's Signature:** [Signed]

Chapter 4: Bank Reconciliation Principles

4.1 Causes of Disparity between Cash Book and Pass Book

Every business maintaining a commercial current account receives a periodic **Bank Pass Book** or Bank Statement from its bank. In theory, because the bank statement is the mirror image of the firm's Cash Book Bank column, the bank balance shown in the Cash Book should exactly equal the balance shown in the Pass Book on any given date. In practical reality, the two balances rarely agree due to **Timing Differences** and **Omission Errors**:

- *1. Cheques Issued by the Firm but Not Yet Presented for Payment:* Creditors are issued cheques and credited in the Cash Book immediately. However, creditors may take days or weeks to deposit them, creating a temporary state where Cash Book balance is lower than Pass Book balance.
- *2. Cheques Deposited into the Bank but Not Yet Cleared:* Customer cheques are debited in the Cash Book on the date of deposit. The banking clearing house requires 2 to 3 days to credit funds, meaning Pass Book balance is temporarily lower than Cash Book balance.
- *3. Bank Charges and Interest Debited by Bank:* Banks automatically deduct ledger folio fees, ATM charges, and overdraft interest, notifying the firm only via month-end statements.
- *4. Direct Collections and Interest Credited by Bank:* Dividends or customer electronic NEFT payments deposited directly into the bank account without immediate advice to the firm's accountant.
- *5. Direct Debits under Standing Instructions:* Automatic insurance premiums, loan EMIs, or utility bill debits executed by the bank under standing mandates.
- *6. Dishonour of Cheques or Bills Discounted:* Customer cheques deposited that bounce due to insufficient funds, which the bank immediately debits back against the account.

4.3 Bank Reconciliation under Bank Overdraft (Unfavourable Balance)

When an enterprise operates an authorized Bank Overdraft facility, its bank balance in the Cash Book reflects a **Credit Balance (Overdrawn / Unfavourable)**. In a bank reconciliation statement starting with an Overdraft as per Cash Book, the direction of

additions and deductions requires rigorous logical application:

Transaction Nature	Favourable Balance (Starting with Dr. Cash Book)	Overdraft Balance (Starting with Cr. Cash Book)
Cheques issued but not presented	**ADD** (Increases Cash Book balance to match Pass Book)	**LESS** (Reduces overdraft debt balance)
Cheques deposited but not cleared	**LESS** (Reduces Cash Book balance to match Pass Book)	**ADD** (Increases overdraft debt balance)
Direct payments by customer into bank	**ADD** (Increases cash balance)	**LESS** (Reduces overdraft liability)
Bank charges / Overdraft interest debited	**LESS** (Reduces cash balance)	**ADD** (Increases overdraft liability)

4.3.1 Comprehensive Worked Problem: Bank Overdraft Reconciliation

To demonstrate the mathematical reconciliation of an overdrawn bank account, consider the records of Precision Engineers on July 31, 2024. The Cash Book indicates an **Overdraft (Credit) balance of Rs 55,000**. Comparison with the SBI Pass Book reveals the following discrepancies:

- 1. Cheques issued to creditors totaling Rs 28,000 were not presented for payment at the bank until August.
- 2. Cheques deposited into bank totaling Rs 36,000 were cleared by the bank only on August 3.
- 3. Bank debited bank overdraft interest of Rs 3,200 and incidental account maintenance charges of Rs 400 directly in the Pass Book.
- 4. A credit customer directly deposited Rs 14,000 into the bank account via NEFT, recorded only in the Pass Book.
- 5. Direct debit for electricity charges Rs 5,500 paid by the bank under standing mandate, not entered in the Cash Book.
- 6. A customer cheque for Rs 6,000 deposited on July 20 was dishonoured by the drawee bank; bank returned the unpaid cheque with a debit note, but no entry was passed in the Cash Book.

Particulars of Discrepancy	Amount (Rs)
Bank Overdraft as per Cash Book (Credit / Unfavourable)	**55,000**
Add: Items increasing Overdraft Debt:	
1. Cheques deposited into bank but not yet cleared/credited by bank	36,000
2. Bank overdraft interest (Rs 3,200) and bank charges (Rs 400) debited by bank	3,600
3. Direct debit for electricity charges paid by bank under standing mandate	5,500
4. Dishonour of customer cheque previously credited, debited back by bank	6,000
Sub-Total Additions	**+ 51,100**
Total	**1,06,100**
Less: Items reducing Overdraft Debt:	
1. Cheques issued to suppliers but not yet presented for payment	(28,000)
2. Direct customer deposit received into bank account via NEFT	(14,000)
Sub-Total Deductions	**- 42,000**
Bank Overdraft as per Bank Pass Book (Debit / Overdrawn)	**Rs 64,100**

4.5 Treasury Operations: Cash Forecasting and Float Optimization

Modern corporate financial controllers manage cash balances through disciplined treasury protocols that optimize liquidity while minimizing idle non-interest-bearing funds:

- **Daily Cash Position Report:** Every morning, the treasury team aggregates opening bank balances across all commercial bank accounts, subtracts cheques and electronic payments scheduled for release that day, and adds anticipated customer collections to establish the net daily cash surplus or deficit. Surpluses are immediately swept into overnight interest-bearing money market mutual funds (Sweep Accounts).
- **Float Management and Dynamics:** *Float* represents the total value of funds tied up during the temporal delay between the initiation of a payment and its final banking clearance:
  - *Collection Float (Incoming):* The delay between a customer mailing or issuing a cheque and the funds becoming usable in the firm's bank account (Mail Float + Processing Float + Availability / Clearing Float). Corporate management seeks to **minimize collection float** through electronic payment gateways (UPI, NACH) and Lockbox Banking systems (where customer payments are mailed directly to local post office boxes cleared multiple times daily by the bank).
  - *Disbursement Float (Outgoing):* The delay between the firm issuing a cheque and the funds being deducted from its bank account. Enterprises strategically **maximize disbursement float** by utilizing centralized disbursement bank accounts to prolong cash retention within the firm.

4.4 Modern Electronic Banking Mechanisms and Internal Controls

Contemporary commerce has largely replaced paper cheques with real-time electronic fund transfer platforms:

- **NEFT (National Electronic Funds Transfer):** Operates on half-hourly batch clearing cycles 24/7/365, suitable for routine vendor payments and employee salary disbursements.
- **RTGS (Real-Time Gross Settlement):** Continuous, real-time gross settlement of high-value funds (mandatorily ≥ Rs 2,00,000 in India) with zero clearing house delay.
- **IMPS and UPI (Unified Payments Interface):** Instant mobile payments operating 24/7, widely deployed for retail customer transactions.
- **Corporate Cash Control Systems:** Enterprises implement two-factor authentication, dual authorization workflows (maker-checker controls where one accountant enters transactions and a finance manager authorizes payments), and daily automated electronic bank statement reconciliations via ERP API integration.

4.2 Summary of Cash Book Governance

The Cash Book serves as the operational fortress safeguarding enterprise liquid liquidity. By functioning as both a journal and a ledger, it eliminates redundant posting while providing real-time visibility over cash and bank reserves. The Three Column format elegantly integrates cash discounts into the transaction stream, while contra entries maintain mathematical equilibrium between office cash drawers and commercial banking portals. The Imprest Petty Cash system establishes unyielding internal control over routine operational expenditures, ensuring full audit compliance across the organizational hierarchy.

Chapter 4: Advanced Banking Reconciliation and Overdraft Mechanics

4.1 Bank Reconciliation Under Overdraft (Unfavorable) Conditions

An overdraft occurs when a commercial enterprise withdraws funds exceeding its credit balance, resulting in a temporary borrowing from the bank. Under bank overdraft conditions, the cash book exhibits a credit balance, while the bank passbook (bank statement) reflects a debit balance. Preparing a Bank Reconciliation Statement under overdraft requires rigorous sign discipline:

Transaction / Cause of Discrepancy	Starting with Overdraft as per Cash Book	Starting with Overdraft as per Pass Book
Cheques issued but not yet presented for payment	ADD to Overdraft Balance	DEDUCT from Overdraft Balance
Cheques deposited/paid in but not yet cleared/collected	DEDUCT from Overdraft Balance	ADD to Overdraft Balance
Interest on overdraft charged directly by bank	DEDUCT from Overdraft Balance	ADD to Overdraft Balance
Direct collections made by bank on behalf of client	ADD to Overdraft Balance	DEDUCT from Overdraft Balance

DegreeLive

Transaction / Cause of Discrepancy	Starting with Overdraft as per Cash Book	Starting with Overdraft as per Pass Book
Direct debits / standing orders paid by bank	DEDUCT from Overdraft Balance	ADD to Overdraft Balance
Cheque deposited returned dishonored by bank	DEDUCT from Overdraft Balance	ADD to Overdraft Balance

4.2 Comprehensive Worked Illustration: Overdraft BRS

On 31st March 2025, the Cash Book of Apex Retailers showed an overdraft balance of Rs 48,000. On comparing with the Bank Statement, the following differences were discovered:

1. Cheques paid into the bank amounting to Rs 24,000 on 28th March, of which cheques of Rs 14,000 were credited in April 2025.
2. Cheques issued totaling Rs 36,000, of which cheques worth Rs 22,000 were presented for payment on 4th April 2025.
3. Bank charges of Rs 850 and interest on overdraft of Rs 3,200 were debited in the passbook but not yet entered in the cash book.
4. A dividend of Rs 6,500 on shares was collected directly by the bank and recorded in passbook only.
5. A cheque of Rs 4,200 deposited was dishonored by the customer's bank; no advice had been received by Apex Retailers.

Solution: Bank Reconciliation Statement as on 31st March 2025

Particulars	Amount (Rs)	Amount (Rs)
Overdraft balance as per Cash Book (Credit)		**48,000**
Add:		
1. Cheques issued but not yet presented for payment (Rs 22,000)	22,000	
2. Dividend collected directly by bank not in cash book	6,500	**28,500**
Sub-total		**76,500**
Less:		
1. Cheques paid in but not cleared (credited in April)	14,000	
2. Bank charges debited in passbook only	850	
3. Interest on overdraft charged by bank	3,200	
4. Cheque deposited returned dishonored	4,200	**(22,250)**
Overdraft balance as per Bank Statement / Pass Book (Debit)		**54,250**

4.3 The Adjusted Cash Book Approach

In modern corporate accounting and statutory audit practice, preparing a BRS directly without adjusting the cash book is considered inadequate. Proper professional procedure requires that the Cash Book must first be updated by passing adjusting journal entries for all omissions, errors committed in the Cash Book itself, and legitimate bank charges/credits:

- **Step 1: Amend the Cash Book:** Enter items that appear in the bank statement but were omitted in the cash book (e.g., bank interest, dividend collections, standing orders, direct customer deposits, and bank charges). Correct all clerical errors made by the firm's bookkeeper.
- **Step 2: Derive the Corrected Cash Balance:** Balance the amended cash book to arrive at the true closing bank balance for financial reporting.
- **Step 3: Prepare BRS on Residual Timing Differences:** The BRS is then drafted using only unpresented cheques, uncleared deposits, and any errors made by the bank itself. This eliminates recurring book discrepancies.

DegreeLive

Chapter 5: Electronic Banking and Payment Systems Accounting

5.1 Mechanics of NEFT, RTGS, IMPS, and UPI

Corporate financial management in India relies extensively on Reserve Bank of India (RBI) regulated electronic payment systems. Each platform has distinct operational parameters and accounting touchpoints:

Electronic System	Settlement Mechanism	Value Threshold	Accounting Verification
NEFT (National Electronic Funds Transfer)	Batch settlement on half-hourly intervals operating 24x7x365.	No minimum or maximum statutory limits for retail transactions.	UTR (Unique Transaction Reference) 16-digit alphanumeric code.
RTGS (Real Time Gross Settlement)	Continuous, immediate gross settlement transaction-by-transaction.	Statutory minimum of Rs 2,00,000 per transaction; no upper cap.	22-character UTR code for high-value treasury confirmation.
IMPS (Immediate Payment Service)	Instant real-time 24x7 interbank electronic transfer via NPCI.	Statutory cap up to Rs 5,00,000 per day per account.	RRN (Retrieval Reference Number) 12-digit numeric tracking.
UPI (Unified Payments Interface)	Virtual Payment Address (VPA) instant settlement via NPCI framework.	Standard limit Rs 1,00,000 to Rs 5,00,000 depending on merchant class.	UPI Transaction ID mapped against merchant gateway settlement reports.

5.2 Accounting for Payment Gateway Settlements and Merchant Discount Rates

E-commerce and modern omnichannel retail firms do not receive customer remittances gross in their bank accounts. When an online customer purchases goods worth Rs 10,000 via credit card or UPI gateway, the payment aggregator (e.g., Razorpay, PayU, CCavenue) deducts a Merchant Discount Rate (MDR) plus GST before transferring net proceeds to the merchant's escrow/current account:

```
Net Remittance Credited = Gross Customer Payment - Gateway MDR Fee - Applicable GST (18% on MDR)
```

Example: Sale of Rs 10,000 subject to 2% MDR fee. MDR = Rs 200, GST on MDR @ 18% = Rs 36. Net bank credit = Rs 9,764.
The standard compound journal entry passed in the merchant's financial books reflects the full transaction:

Journal Entry Accounts	Debit (Rs)	Credit (Rs)
Bank Current Account (Dr.) [Net proceeds received]	9,764	-
Payment Gateway Commission Expense Account (Dr.) [Operating expense]	200	-
Input CGST / SGST Account (Dr.) [Input tax credit on MDR fee]	36	-
To Sales Revenue Account (Cr.) [Gross turnover recognized]	-	10,000

Chapter 6: Analytical Petty Cash and Internal Cash Governance

6.1 Comprehensive Format of Analytical Petty Cash Book under Imprest System

In medium and large-scale enterprises, routine minor disbursements are delegated to a Petty Cashier under the Imprest System to relieve the Head Cashier from excessive administrative burden. An analytical petty cash book features distinct analysis columns for recurring operational expense categories:

Date & Voucher	Particulars of Expense	Total (Rs)	Postage (Rs)	Conveyance	Stationery	Sundries (Rs)
Jan 01 (V01)	Speed post and courier charges for legal notices	450	450	-	-	-
Jan 03 (V02)	Auto-rickshaw fare for sales executive client visit	280	-	280	-	-
Jan 05 (V03)	Printing paper reams and ballpoint pens for office	620	-	-	620	-
Jan 08 (V04)	Tea and mineral water for quarterly board meeting	350	-	-	-	350
Jan 12 (V05)	Metro rail cards recharge for audit trainees	500	-	500	-	-
Jan 15 (V06)	Office cleaning detergent, sanitizer, and towels	400	-	-	-	400
Total Period	**Total Expenses Disbursed for Re-imbursement**	**2,600**	**450**	**780**	**620**	**750**

6.2 Internal Financial Controls and Fraud Prevention in Cash Management

Cash is the most liquid and vulnerable asset on a commercial entity's balance sheet. Robust internal control frameworks require strict segregation of operational and custodial functions:

- **Dual Authorization Protocol:** All cheques exceeding pre-set financial thresholds (e.g., Rs 50,000) mandatorily require two authorized signatories (e.g., Managing Director and Chief Financial Officer). Single-signatory discretion creates unacceptable exposure to embezzlement.
- **Surprise Cash Audits:** Independent internal audit staff must conduct unannounced physical counts of petty cash boxes and Head Cashier vaults at irregular intervals, reconciling physical currency against general ledger cash records.
- **Mandatory Daily Bank Deposits:** Cash collections received across physical retail counters or sales depots must be deposited intact into the scheduled commercial bank current account on the same day or the morning of the next business day. Retaining operational cash on premises overnight for subsequent expenses violates core internal control principles.
- **Strict Policy on Stale and Post-Dated Cheques:** Cheques issued by or presented to the enterprise must be tracked against the statutory 3-month validity window under Indian banking regulations. Stale cheques must be written back, and post-dated cheques must be placed under safe custody until their due presentation date.

DegreeLive