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Accounting & Financial Management for Bankers

Quick Revision Capsule

Module A: Accounting Principles and Processes

Chapters 1-11 · 38 pages

JAIIB | AFM | Module A | JAIIB: 2026-27

Fact-checked & current

Up to date till 30 June 2026.

Chapter-wise key points

Crisp bullets and summary tables for each chapter.

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CHAPTER 1. DEFINITION, SCOPE AND ACCOUNTING STANDARDS INCLUDING IND AS

Introduction to Accounting

- **AICPA (1941)**: accounting is an **art**; **AAA (1966)**: identifying, measuring, communicating information.
- Books: **s.128 Companies Act, 2013**. **Income-tax Act, 2025** (from **1 April 2026**): **s.62** books (old s.44AA), **s.276** method/ICDS (old s.145).
- **s.2(40)**: Balance Sheet, P&L, Cash Flow Statement, SOCE (where applicable), notes. **OPC, small, dormant** companies need no cash flow statement.
- Fund flow: only an **analytical tool** since **AS 3 revised 1997**.

Evolution of Accounting

- **Luca Pacioli**, Summa, **1494**, Venice. India: **Kautilya's Arthashastra**; **Bahi-Khata** (Mahajani/Marwari/Deshi Nama).
- **BRSR**: top **1,000** listed companies. Inflation accounting: **CPP** (general index), **CCA** (replacement cost).
- **Fair value (Ind AS 113)**: **exit price**; **Level 1** quoted, **Level 2** observable, **Level 3** unobservable inputs.

Concepts, Conventions and GAAP

- **AS 1 assumptions**: **going concern, consistency, accrual**; disclose only if **not** followed. Policy considerations: **prudence, substance over form, materiality**.
- **Conceptual Framework (Ind AS) 2020**: fundamental = **relevance, faithful representation**.

Standard-setting in India

- **ASB of ICAI**: **21 April 1977**; binds companies once **MCA notifies under s.133**, after **NFRA** examines.
- **s.129(5)** deviation disclosed with reasons, effect; **s.134(5)(a)** Directors' Responsibility Statement; **s.143(3)(e)** auditor.
- **Companies (AS) Rules, 2021** (notified **23 June 2021**, periods from **1 April 2021**; amended up to **10 March 2026**). **Companies (Ind AS) Rules, 2015** (**16 February 2015**).
- **NFRA**: **s.132**, from **1 October 2018**, replaced **NACAS** (s.210A, 1956 Act); can debar auditors **six months to ten years**.
- **SMC/MSME**: unlisted, not bank/FI/insurer, turnover up to **Rs 250 crore**, borrowings up to **Rs 50 crore**. AS 3, 17, 24 not for MSMEs. **Banks**: always Large Entities/non-SMCs.

Accounting Standards at a Glance

- **27 AS** in force: AS 1-29 except **AS 6** (into AS 10, 2016) and **AS 8** (into AS 26). AS 30-32 withdrawn **2016**.
- **AS 21** line-by-line; **AS 23** equity method; **AS 27** proportionate consolidation.

Key Standards Explained

Key AS Rules and Results

AS	Rule	Worked result
2	Lower of cost and NRV, item-wise; **no LIFO**	Rs 95,000
3	Cash equivalents **3 months** or less	Net operating cash Rs 4,60,000
7	Percentage of completion only	60%: revenue 600, profit 150 (Rs lakh)
10	Fall: surplus first, then P&L	Fall 250: reserve 150, P&L 100
11	Closing rate for monetary items	Loss Rs 15,000; then gain Rs 5,000
20	Basic and diluted on P&L face	Basic Rs 7.69; diluted Rs 7.12
22	Timing differences	DTL Rs 15,000
28	Higher of NSP and value in use	Loss Rs 24,520

- **AS 4**: proposed dividend not a liability. **AS 9**: no interest on NPAs until received.
- **AS 16**: qualifying asset ordinarily **12 months**. **AS 26**: life presumed not over **10 years**.
- **AS 29**: contingent asset **not disclosed** in statements, **Board's report** if inflow probable.

Accounting Standards in Banks

- **RBI (Commercial Banks – Financial Statements: Presentation and Disclosures) Directions, 2025**, issued **28 November 2025**. **Form A/Form B**, Third Schedule, BR Act, 1949; **12 schedules**.
- **AS 5**: prior period disclosed if over **1%** of total income/expenditure or net profit before tax. **AS 13** not applied; **AS 28** fixed assets only.

Indian Accounting Standards (Ind AS)

- IFRS-based, under **s.133**; **convergence** with carve-outs/carve-ins.
- **Ind AS 117 replaced 104 (August 2024)**.

Ind AS Roadmap

Phase	Who	From
Companies I	Net worth **Rs 500 crore+**	**1 Apr 2016**
Companies II	Other listed; unlisted Rs 250-500 crore	**1 Apr 2017**
NBFCs I / II	Rs 500 crore+ / listed and Rs 250-500 crore	**1 Apr 2018 / 2019**
Banks (SCBs)	Deferred till further notice	Not yet
Insurers	As per IRDAI	**1 Apr 2026**

- Ind AS: extraordinary items **prohibited**; goodwill **not amortised**.

Ind AS for Banks, NBFCs and Insurers

- SCBs: deferred by RBI on **22 March 2019** till further notice; still on Indian GAAP as on 30 June 2026.
- **RBI ECL Directions, 2026**: **issued April 2026 (dated 27 April 2026), effective 1 April 2027**. **Stage 1** 12-month ECL; **Stages 2-3** lifetime; SICR presumed at **more than 30 days** past due.
- NBFCs: where ECL is below prudential provisions, gap to **impairment reserve**. Insurers: Ind AS from **FY 2026-27**, one-time **one-year forbearance**.

IFRS and US GAAP

- **IASC 1973**, replaced by **IASB 2001**; **IFRS 18, 19** effective **1 January 2027**.
- **FASB 1973**, rules-based. **LIFO** permitted under US GAAP, prohibited under IFRS; US GAAP uses **CECL**, IFRS 9 three-stage ECL.

Transfer Pricing

- **Minimum TP = Variable cost + Opportunity cost**.
- Example: spare capacity **Rs 60,000**; full capacity 60,000 + 35,000 = **Rs 95,000**; ceiling market **Rs 1,00,000**.
- Tax: **arm's length price**, **Income-tax Act, 2025 ss.161-173** (old ss.92-92F); methods **s.165** (CUP, resale, cost plus, profit split, TNMM, other).

Most Likely in Exam

- ASB of ICAI: 21 April 1977; NFRA under s.132 from 1 October 2018.
- 27 AS in force; AS 7 only percentage of completion.
- AS 28 impairment loss: Rs 24,520; AS 29 contingent asset in Board's report.
- Ind AS Phase I: net worth Rs 500 crore, 1 April 2016; banks deferred 22 March 2019.
- RBI ECL Directions effective 1 April 2027; SICR at more than 30 days past due.
- Minimum transfer price = variable + opportunity cost; ALP methods in s.165.

CHAPTER 2. BASIC ACCOUNTANCY PROCEDURES

Introduction

- **Book-keeping**: journal and ledger (clerical); **accounting**: also classifying, summarising, interpreting; **accountancy**: the discipline. Definition: **AICPA (1941)**.
- **Journal** = book of original (prime) entry; **ledger** = book of final entry.
- **AS**: Companies (Accounting Standards) Rules, **2021**; **Ind AS** (IFRS-converged): Rules, **2015**. ASB formulates, **NFRA** recommends, **MCA** notifies.
- RBI deferred Ind AS for SCBs on **22 Mar 2019** "till further notice"; as on **30 Jun 2026** banks follow AS plus RBI directions.

Accounting Concepts and Conventions

- **Concepts**: recording assumptions; **conventions**: full disclosure, materiality, conservatism, consistency.
- **AS 1** fundamental assumptions: **going concern, consistency, accrual**; disclose only if **not followed**. Policy considerations: **prudence, substance over form, materiality**.
- **Ind AS 1**: accrual except cash flow information; no offsetting; at least annual reporting.
- **Conceptual Framework**: fundamental qualities **relevance** and **faithful representation**; enhancing: comparability, verifiability, timeliness, understandability.

Entity, Money Measurement and Cost Concepts

- **Business entity**: **capital is a liability** to the owner; drawings reduce capital.
- **Money measurement** ignores non-money facts, assumes stable rupee; only exception **Ind AS 29** (hyperinflation).
- **Cost** includes all costs to working condition: machine **Rs 44 lakh**; recoverable GST excluded.
- Carrying amount = Cost – Accumulated depreciation – Impairment losses. Revaluation allowed (**AS 10 (Revised)/Ind AS 16**); fair value under **Ind AS 109**.
- Banks: HFT/AFS investments at fair value, HTM at amortised cost.

Dual Aspect and the Accounting Equation

- **Assets = Liabilities + Capital**; expanded: A = L + C + Revenue – Expenses – Drawings.
- Ledgerleaf: **Rs 10,65,000** = Rs 80,000 + **Rs 9,85,000**.
- **Modern rules**: increases in assets, expenses, drawings are **debits**; liabilities, capital, revenue are **credits**.

Realisation and Revenue Recognition

- Revenue when performed and customer liable to pay, not on cash receipt.
- **AS 9**: goods when **risks and rewards** pass; **interest on time-proportion**; dividends when right established.

- Goods on approval: sale on acceptance or retention past approval period.
- **Ind AS 115** (from **1 Apr 2018**): five steps; revenue when **control** passes.
- **Banks**: accrual on standard advances; **NPA income on cash basis**; unrealised interest reversed (IRACP Directions, 2025, issued **28 Nov 2025**).
- **ECL Directions, 2026**: issued **27 Apr 2026**, effective **1 Apr 2027**; staging framework; not for SFBs, payments banks, LABs; 2025 Directions repealed from that date.

Accounting Period and Matching

- **Matching**: expenses set against revenue they earned, same period.
- Companies: FY ends **31 March** (**s.2(41)**); other year only with **NCLT** approval.
- **Income-tax Act, 2025, s.3** (in force **1 Apr 2026**): single **tax year**.
- Rs 10 lakh loan at 9%: June accrual **Rs 7,500**. Advertising expensed (**AS 26/Ind AS 38**).

Year-end adjustments

Item	Meaning	Shown as
Outstanding expense	Used, not paid	Liability
Prepaid expense	Paid for next period	Asset
Accrued income	Earned, not received	Asset
Income received in advance	Received, earned next period	Liability

Going Concern Concept

- **Ind AS 1**: assessment covers **at least 12 months** from end of reporting period; disclose material uncertainties; if not going concern, disclose fact, basis and reason. Auditor: **SA 570 (Revised)**.
- Rig **Rs 12,00,000**: **Rs 1,20,000** a year rises to **Rs 2,50,000** on planned 4-year closure; change in estimate, still a going concern.

Accrual Basis and Cash Basis

- **Companies Act, 2013, s.128(1)**: **accrual basis and double entry**.
- **Income-tax Act, 2025, s.276** (old s.145): cash or mercantile **regularly employed**, subject to **ICDS**.
- Hybrid: income on cash, expenses on accrual.
- Cloud kitchen: cash profit **Rs 2,20,000**, accrual **Rs 2,37,000**.

Accounting Conventions

- **Disclosure**: companies **s.129, Schedule III**; banks **Forms A and B**, Third Schedule, **BR Act s.29**. No secret reserves.

- **Materiality**: **no fixed cut-off**; Ind AS firms disclose "material accounting policy information" from **1 Apr 2023**.
- **Conservatism**: stock at **lower of cost and NRV**, item by item (**AS 2/Ind AS 2**): phone stock **Rs 86,000**. Provisions only for probable obligations (**AS 29/Ind AS 37**).
- SLM to **WDV 40%**: FY 2025-26 depreciation **Rs 1,20,000**; past years not recomputed.

Policy versus estimate change

Point	Policy change	Estimate change
Example	FIFO to weighted average	Depreciation method or useful life
Applied	Ind AS 8: retrospectively; AS 5: effect disclosed in year of change	Prospectively

Double Entry and the Golden Rules

- **Double entry**: receiving aspect debited, giving aspect credited; total debits = total credits.
- **Single entry** profit = Closing capital − Opening capital + Drawings − Fresh capital.
- Agreed trial balance misses errors of **complete omission, principle, compensating**, wrong account on correct side.
- **Personal**: natural, artificial, representative; **real**: assets; **nominal**: expenses, incomes.

Golden rules

Type	Debit	Credit
Personal	The receiver	The giver
Real	What comes in	What goes out
Nominal	Expenses and losses	Incomes and gains

Journal and Ledger

- **Journal columns**: Date, Particulars, **L.F.**, Debit, Credit.
- Ledger debit entries begin **"To"**, credit **"By"**; **Balance c/d** on lighter side, **b/d** opposite.
- Ledgerleaf: journal total **Rs 20,75,000**; bank balance **Rs 5,45,000** (debit); trial balance **Rs 13,80,000** each side.

Most Likely in Exam

- AS 1: going concern, consistency, accrual; prudence is not one.
- Capital is a liability (business entity concept).
- s.128(1): accrual basis and double entry.
- NPA income only when actually received.
- Depreciation method change: estimate, prospective.
- Stock at lower of cost and NRV.

CHAPTER 3. MAINTENANCE OF CASH, SUBSIDIARY BOOKS AND LEDGER

Introduction

- **Bookkeeping** records and classifies; **accounting** also summarises, interprets and reports.
- **Double entry**: equal debit and credit for every transaction, so the trial balance is possible.
- **Cash book**: book of original entry and also the Cash/Bank A/c; the **only subsidiary book that is also a ledger**.

Record Keeping Basics

- Cycle: **recording, classifying, summarising**.
- Source documents: cash memo, invoice, receipt, pay-in-slip; **debit note** with purchase returns, **credit note** with sales returns.
- Voucher number goes in the cash book's **V.No.** column; every CBS entry has a cash, clearing or transfer voucher.

Classification of Accounts and Rules of Debit and Credit

Golden rules

Type	Sub-types / examples	Debit	Credit
Personal	Natural, artificial (SBI), **representative** (Prepaid Rent)	Receiver	Giver
Real	Tangible (cash), **intangible** (goodwill, patents)	What comes in	What goes out
Nominal	Rent, wages, commission received	Expenses, losses	Incomes, gains

- Modern approach: **Assets = Liabilities + Capital**; assets and expenses rise by debit; liabilities, capital, revenues by credit. **Drawings** debited (reduce capital). Both approaches give the same entry.

Journal

- Columns: **Date, Particulars, L.F., Dr, Cr**; without a **narration** an entry is incomplete. **Compound** entry: three or more accounts.
- Free samples: **Advertisement Dr, To Purchases**; fire loss: **Loss by Fire Dr, To Purchases**.
- Opening entry: assets **Rs 8,00,000** - creditors **Rs 1,80,000** = Capital **Rs 6,20,000**.
- **Trade discount never entered**; cash discount recorded. Rs 2,00,000 less 10% = **Rs 1,80,000**; 2% cash discount **Rs 3,600**; dealer pays **Rs 1,76,400**.

Ledger

- Book of **final entry**, by account. Debit side "To", credit side "By". Ledger has **J.F.**; journal and cash book have **L.F.**
- A **real account cannot normally have a credit balance**. Nominal balances **closed** to Trading and P&L; personal and real go to Balance Sheet.
- Illustration: Bank **Rs 2,80,000** Dr; trial balance agrees at **Rs 5,55,000**.

Subsidiary Books

What goes into which book

Book	Records / document	Each item	Total
Purchases	Credit purchases of goods	Supplier Cr	Purchases Dr
Sales	Credit sales of goods	Customer Dr	Sales Cr
Purchases Returns (Outward)	**Debit note**	Supplier Dr	Returns Cr
Sales Returns (Inward)	**Credit note**	Customer Cr	Returns Dr
Bills Receivable / Payable	Bills accepted	Debtor Cr / Creditor Dr	B/R Dr / B/P Cr

- Assets bought on credit go to the **Journal Proper**, not the Purchases Book. GST columns make a **columnar book**.
- Solar PV modules: GST **5%** (CGST 2.5% + SGST 2.5%), rate changes effective **22 September 2025**. Feb 2026 purchases net **Rs 8,06,000**, total **Rs 8,46,300**.
- **Journal Proper**: opening, adjusting, rectification entries, free samples, fire loss, bad debts, dishonour of bills.

Cash Book

- Receipts **debit**, payments **credit**. Cash column **never has a credit balance**; bank column may (**overdraft**).
- Forms: **single, double, three column, petty cash**. Single column has **L.F.**, not J.F.

- Tiffin Tales: receipts **Rs 41,100** - payments **Rs 33,550** = cash **Rs 7,550**. Debit-side items are posted to the **credit** of ledger accounts.

Double and Three Column Cash Books

- **Contra entry** (cash deposited into bank; cash withdrawn for office use): marked **"C"**, **not posted**.
- Not contra: cheque **banked the same day**; cheque **endorsed** to a creditor (no bank entry); owner's personal withdrawal (**Drawings**).
- Bank charges Rs 500 + 18% GST = **Rs 590**. A deposit is a **credit in the pass book**.
- Discount columns: **totalled, not balanced**; Dr total to **Discount Allowed A/c**, Cr total to **Discount Received A/c**. March 2026: **Rs 4,800** allowed, **Rs 6,000** received.

Petty Cash Book and Imprest System

- Only receipt: money from the **chief cashier**. **Analytical** book: Total column balanced, analysis columns only totalled.
- **Imprest**: reimburse **exactly the amount spent**. Imprest **Rs 5,000**, spent **Rs 3,930**, balance **Rs 1,070**, reimbursement **Rs 3,930**.
- Only column totals posted: expenses Dr, **Petty Cash A/c** Cr.

Maintaining Cash and Books in Practice

- Branch cash under **dual custody**, verified daily. Limits under **Income-tax Act, 2025** (in force **1 April 2026**) continue 1961 Act limits.

Cash limits (30 Jun 2026)

Rule	Limit	Section
Cash expense	Disallowed if **over Rs 10,000** per person per day (**Rs 35,000** goods carriages)	old s.40A(3)
Cash receipt	**Rs 2 lakh or more** from one person in a day, one transaction or one event prohibited	old s.269ST
Cash loan/deposit taken	**Rs 20,000 or more** prohibited	s.185 (old s.269SS)
Cash loan/deposit repaid	**Rs 20,000 or more** prohibited	s.188 (old s.269T)
E-payment modes	Required if turnover exceeded **Rs 50 crore** in preceding tax year; penalty **Rs 5,000/day** (old s.271DB)	s.187 (old s.269SU)

- Breach of receipt or loan limits: penalty **equal to the amount** (old ss.271D, 271DA, 271E); UPI and bank payments outside limits.

- **Companies Act, 2013, s.128**: accrual, double entry. **Rule 3, Companies (Accounts) Rules, 2014** (w.e.f. **11 August 2022**): daily backup on servers in India.
- **Audit trail** mandatory from FYs beginning on or after **1 April 2023**; books preserved **eight financial years**.

Most Likely in Exam

- Cash book is the only subsidiary book that is also a ledger.
- Prepaid Rent is **representative personal**; goodwill is **intangible real**.
- Trade discount is never recorded.
- Contra entries are marked "C" and not posted.
- Imprest: reimburse **Rs 3,930** spent, not Rs 5,000.
- Cash receipt **Rs 2 lakh or more** prohibited; books kept **8 years**.

CHAPTER 4. BANK RECONCILIATION STATEMENT

Introduction

A **BRS** explains, on a stated date, the gap between the cash book bank column and the passbook, starting from one balance and reaching the other.

- A **statement, not an account**: no posting; only corrections it reveals go into the cash book. Prepared by the **account holder**.
- Under **AS 3 / Ind AS 7**, demand deposits are **cash**, not cash equivalents (normally maturing **within three months** of purchase).
- **Favourable**: cash book **Dr** = passbook **Cr** (positive). **Overdraft**: cash book **Cr** = passbook **Dr** (negative, in brackets).

Bank Transactions in the Cash Book

- **Double-column cash book**: receipts debited, payments credited; cash deposited/withdrawn is a **contra entry**, marked **"C"**.
- UPI and NEFT receipts are often entered late and cause differences.

The Passbook and Bank Statement

- The firm's account is a **liability** of the bank: deposits credited, payments debited.
- Passbook is the **mirror image** of the bank column, for **direction of entries**, not always balances.

Need for Reconciliation

- Main reason for differences: **timing**. The firm records at once; the bank records only when money moves.
- **CTS** covers all bank branches since **30 September 2021**; no outstation route for CTS cheques.

- Cheque deposited after the bank's cut-off for the presentation session (closes **3 pm**) or on the last day is credited the **next working day**.

CCSR in CTS (30 Jun 2026)

Feature	Position	Date
Circular	RBI/2025-26/73 (two phases); modified by RBI/2025-26/156	13 Aug 2025; 24 Dec 2025
Phase 1	Live; continuous scanning	4 Oct 2025
Sessions	Presentation 9 am-3 pm; confirmation 9 am-7 pm	As revised 24 Dec 2025
Settlement / credit	Hourly from 11 am; credit not later than 1 hour after settlement	Phase 1
Phase 2 (3-hour expiry)	Deferred until further notice	Was due 3 Jan 2026

Causes of Difference

- **Group 1, timing**: issued not presented; deposited not credited (incl. UPI/card settled later); entered but not sent. **Only in BRS**.
- **Stale cheque**: valid **three months** from its date (RBI, effective **1 April 2012**); write back **Bank A/c Dr, To Creditor A/c**.
- **Group 2, bank-first**: debits (charges plus **GST**, OD interest, ECS/NACH, dishonours); credits (direct receipts, interest, collections). Update cash book.
- **s.138 NI Act, 1881**: notice **within 30 days** of return memo; drawer must pay **within 15 days** of notice; **up to two years** and/or fine **up to twice** the amount.
- **Positive Pay** (from **1 Jan 2021**): cheques **Rs 50,000 and above**; may be mandatory for **Rs 5 lakh and above**.
- **Group 3, errors**: own errors corrected in cash book (**wrong side = twice the amount**); bank errors only in BRS.

Item and Cash Book Action

Item	Group	Action in cash book
Cheque not presented / deposit not credited	1	None; show in BRS
Stale cheque (over 3 months)	1 (exception)	Write back: Dr Bank
Charges, OD interest, NACH, dishonour	2	Enter on credit side
Direct receipts, interest/dividend	2	Enter on debit side
Error in cash book	3	Correct the cash book
Error by bank	3	None; show in BRS, report

Steps in Reconciliation

- **Check statement, match, adjust for timing items, correct cash book, agree**.
- **Adjusted bank balance** is notional; **adjusted cash book balance** goes to trial balance and balance sheet.

Methods of Preparing a BRS

- **Plus-and-minus**: other record **higher, add**; **lower, deduct**. Switching starting record or to overdraft **reverses every sign**.
- **A = B** (IIBF textbook): Part A, timing items and bank errors; Part B, cash book errors and bank-only items.

Plus-and-Minus Rules

Item	Start: CB Dr or PB Dr (OD)	Start: PB Cr or CB Cr (OD)
Cheques issued, not presented	Add	Less
Deposited, not credited	Less	Add
Credits only in passbook	Add	Less
Debits only in passbook	Less	Add

Illustrations on BRS

- Favourable: CB **Rs 4,82,500** → passbook **Rs 5,35,655**. Overdraft: CB OD **Rs 2,64,600** → passbook OD **Rs 2,40,000**; A = B = **(Rs 2,45,000)**.
- Errors: net correction **Rs 6,450**; A = B = **Rs 26,045**. Passbook items dated on or before the BRS date are adjusted even if advice comes later.

The Amended Cash Book

- Updated first for **bank-only items** (not bank errors) and **own errors**; BRS keeps timing items and bank errors.
- Dishonour: **Debtor A/c Dr, To Bank A/c**; NACH EMI: **Loan A/c and Interest A/c Dr, To Bank A/c**.
- Illustration: amended **Rs 2,22,756** Dr; passbook **Rs 2,54,256**.

BRS from Extracts of Cash Book and Passbook

- **Same period**: only **uncommon** entries reconcile. **Different periods**: **common** entries reconcile; next-period-only entries **ignored**.

Advantages and Limitations

- Advantages: **accuracy, error detection, true bank balance, fraud control, internal control**.
- Limits: only explains; misses identical errors in both records; depends on frequency. Software matches by **amount, date, UTR / UPI ID**.

Most Likely in Exam

- From CB Dr: add unpresented cheques, deduct deposits not credited.
- CB credit balance = passbook debit balance = overdraft.
- Cheque valid **3 months**; stale cheque written back: Bank A/c Dr.
- Wrong-side carry-forward corrected at **twice** the amount.
- Jan cash book with Feb passbook: use **only common entries**.
- CCSR Phase 1 live **4 Oct 2025**; Phase 2 deferred.

CHAPTER 5. TRIAL BALANCE, RECTIFICATION OF ERRORS AND ADJUSTING AND CLOSING ENTRIES

Trial Balance: Meaning and Purpose

A **trial balance** lists ledger balances, debits and credits, on one sheet to test that the two columns are equal.

- **Kohler**: list of balances or totals to determine equality of posted debits and credits and give a basic summary for financial statements. **R.N. Carter**: ledger balances plus **cash-in-hand and cash-at-bank** from the cash book.
- A **statement, not an account** (no To/By); **as on a date**; working paper, **not required by law**.
- Purposes: arithmetical check, summary for final accounts, finding errors, comparison. Agreement is only **prima facie** proof.

Format and Placing of Balances

- Columns: S. No., Account, **L.F.**, Debit, Credit. **DEAD CLIC**: Debit = Expenses, Assets, Drawings; Credit = Liabilities, Income, Capital.
- **Debit**: drawings, opening stock, sales returns, discount allowed, bad debts, prepaid expenses, accrued income.
- **Credit**: provisions, purchase returns, discount received, outstanding expenses, income received in advance, **bank overdraft**.
- **Closing stock** normally not shown; **Dr** only when purchases are adjusted for it. Arka specimen totals **Rs 29,20,000**.

Methods and Types of Trial Balance

Three Methods of Preparation

Method	Entered	Columns	Use
Totals (gross)	Dr and Cr totals	2	Rare
Balances (net)	Net balance	2	Most common
Totals-cum-balances (compound)	Both	4	Rare; most complete

- Totals method total = entries posted (**journal total** if no opening balances); nil-balance accounts appear only here. Tiffin Tales: totals **Rs 13,38,000**, balances **Rs 7,90,000**.
- Stages: **unadjusted**, **adjusted** (basis of final accounts), **post-closing** (only real and personal accounts).

Limitations and Disagreement

- **Not revealed**: complete omission, original-entry error, wrong account on correct side, principle, compensating, complete reversal, duplication.
- **Revealed**: wrong casting/balancing, wrong amount or side in posting, partial omission, balance omitted or in wrong column.

Classification of Errors

- By cause: **clerical** (omission, commission, compensating, duplication) or **principle**. By effect: **one-sided** or **two-sided** (TB agrees if amounts equal).
- **Partial omission** (sale not posted to customer) affects TB; **complete omission** does not.
- **Commission**: wrong posting/casting affects TB; wrong account of same class (Ravi for Ravindra) does not.
- **Principle**: capital expense to revenue understates profit; revenue expense capitalised overstates it.

- **Compensating**: errors cancel. **Duplication**: reverse the extra entry.

Location of Errors

- Re-add TB first; last resort, check every posting.
- **Half-difference test**: wrong-side posting shifts totals by **twice** the amount.
- **Divisible by 9**: **transposition** (74 as 47) or **slide** (4,500 as 450). Swap difference = 9 × digit gap × place value.
- Difference **Rs 1,800**: half-difference **Rs 900**; 1,800 ÷ 9 = 200 (credit Rs 2,000 entered as Rs 200).

Rectification of Errors

- Rectify, **never erase** (CBS: reversal voucher).
- One-sided: before TB, **explanatory posting**; after TB, journal entry with **Suspense A/c**; after final accounts, nominal accounts via **P&L Adjustment A/c**.
- **Two-sided**: always journal entry. Credit purchase Rs 30,000 in sales book: Purchases Dr, Sales Dr, To Nova Cells **Rs 60,000**.
- Wrong-side posting corrected with **double the amount** (Rs 6,000 needs **Rs 12,000**).

Suspense Account and Effect on Profit

- **Debit side short**: difference on Suspense debit; **credit short**: on credit.
- Residual **debit** balance: **assets side**; **credit**: **liabilities side**.
- Greenleaf: difference **Rs 6,280** cleared; profit **Rs 4,80,000** corrected to **Rs 4,92,900**.
- Profit changes only when a **nominal account** is debited (falls) or credited (rises).

Rectification After Books Are Closed

- **P&L Adjustment A/c** (textbook, sole trader) replaces nominal accounts; balance to **Capital** (partners' capital in a firm). Volt EV Spares: net credit **Rs 24,500** to Capital.

Prior Period Error Treatment

Point	P&L Adjustment	AS 5	Ind AS 8
Used by	Sole traders, firms (textbook)	Indian GAAP incl. banks	Ind AS companies
Correction	P&L Adjustment, then Capital	Current P&L, disclosed separately	Restate comparatives/opening balances

- **AS 5** prior period items: income or expenses arising in the current period from errors or omissions of prior periods; nature and amount disclosed separately.
- **Ind AS 8 para 42**: retrospective correction of material errors.

- Banks follow **AS**: RBI deferred Ind AS for SCBs on **22 March 2019** "till further notice"; unchanged on **30 June 2026**.

Adjusting and Closing Entries

- Accrual concept. Prepaid: Prepaid Expense Dr, To Expense. Advance income: Income Dr, To Income Received in Advance.
- Closing stock: Closing Stock Dr, To Trading. Owner's goods: Drawings Dr, To Purchases. Doubtful debts: P&L Dr, To Provision.
- Swift Cloud Kitchen: prepaid insurance **Rs 27,000**, accrued interest **Rs 17,500**, provision **Rs 10,000**.
- **Closing entries** close only **nominal accounts**; net profit to Capital. Prism: gross profit **Rs 6,15,000**, net profit **Rs 1,67,500**, closing capital **Rs 10,47,500**.
- **Opening entry**: assets Dr, To liabilities and capital.

Trial Balance in Banks

- CBS accepts only balanced vouchers; **GL balanced at EOD**: a daily trial balance.
- Old unreconciled suspense/sundry entries: **fraud risk**; RBI norms call for provisions against old unreconciled debits.
- No accrual on NPAs: **recognised only when received**. Final accounts per **Third Schedule, BR Act, 1949**.
- Rs 20,00,000 TD at 6.6% for 2 months: accrued **Rs 22,000**.

Most Likely in Exam

- TB agreement is only prima facie proof.
- Principle, complete omission, compensating errors: TB still agrees.
- Half-difference: wrong side; divisible by 9: transposition/slide.
- Wrong-side posting rectified with double amount.
- Residual Suspense debit: assets side.
- Ind AS 8 para 42: retrospective restatement.

CHAPTER 6. DEPRECIATION AND ITS ACCOUNTING

Introduction

Depreciation (AS 10 (Revised) / Ind AS 16): the systematic allocation of the depreciable amount of an asset over its useful life.

- Only **fixed assets**; **freehold land** not depreciated.
- Depreciable amount = Cost - Residual value; Carrying amount = Cost - Accumulated depreciation - Accumulated impairment.

- Causes: **wear and tear, efflux of time, obsolescence, accidents, depletion**. Temporary market fall is not depreciation; permanent fall = **impairment** (AS 28 / Ind AS 36).
- **s.123 Companies Act, 2013**: dividend only after depreciation per Schedule II.

Standards, Schedule II and Tax Law

- **AS 6 withdrawn**, merged into **AS 10 (Revised)** (MCA, **G.S.R. 364(E), 30 March 2016**).
- Starts when **available for use**; not stopped when merely idle (unless usage method gives nil); estimates reviewed **at least every year-end**.
- **Component approach**: voluntary from **1 April 2014**, mandatory from **1 April 2015**.
- Schedule II gives **lives, not rates**; residual ordinarily **not more than 5%**; double shift **+50%**, triple **+100%** (not NESD).
- Recoverable amount = higher of fair value less costs of disposal and **value in use**; excess carrying amount = impairment loss.
- Tax from **1 April 2026**: **s.33 Income-tax Act, 2025** (old s.32); **block of assets**, WDV; rates in **Income-tax Rules, 2026, Appendix I (rule 25)**; **goodwill not eligible**.
- Used **less than 180 days**: **50%** of rate. **Additional depreciation 20%** on new P&M (manufacturing/power); under 180 days, 10% + 10% next year.

Schedule II Lives and Tax Rates

Asset	Schedule II life	Tax WDV rate
Buildings	60 (RCC, non-factory); 30 (factory)	5% mainly residential; 10% other
Plant and machinery (general)	15 years	15%
Furniture and fittings	10 years	10%
Motor cars (not hire)	8 years	15%
Computers	Servers 6; laptops 3 years	40%
Intangibles	-	25%

Accounting Entries for Depreciation

- **Method 1**: credit Asset A/c. **Method 2**: credit **Provision for Depreciation A/c** (cost less accumulated depreciation, as Schedule III requires).
- On sale, charge depreciation **up to date of sale**; use **Asset Disposal A/c**.
- Closing accumulated depreciation = opening + charge - depreciation on assets sold.

Methods of Depreciation

- Equal: **SLM**. Accelerated: **WDV, DDB, SYD**. Usage: units of production, machine-hour, depletion.

Straight Line Method

- Also **fixed instalment / original cost** method. Annual depreciation = (Cost - Residual) ÷ Life; **rate = depreciation ÷ cost × 100**.
- Rs 5,00,000, scrap Rs 50,000, 5 years: **Rs 90,000**, rate **18%**.
- Demerit: ignores **rising repairs**.

Written Down Value Method

- Also **diminishing / reducing balance**; used for **tax blocks**; book value **never zero**.
- Rate = [1 - ⁿ√(S ÷ C)] × 100; nil S gives 100%, so **Re 1** assumed. Rs 10,00,000, S Rs 64,000, 3 years: **60%**.
- **DDB** = 2 × SLM rate on WDV; **highest year-1 charge** (ATM Rs 5,00,000, 5 years: **40%**, **Rs 2,00,000**).

Other Methods of Depreciation

- **SYD**: sum = n(n + 1) ÷ 2; 10 years = **55**; year 1 = 10/55 × (C - S).
- **Units of production**: (units this year ÷ total units) × (C - S). **Machine-hour**: (C - S) ÷ total hours.
- **Depletion**: (C - Residual) ÷ total reserves, for mines, quarries, oil wells.
- **Annuity**: Cost × [i ÷ (1 - (1 + i)^-n)]; suits **leaseholds**; net charge rises over time.

Depreciation Fund and Replacement

- Depreciation **retains profit but sets no cash aside**; a **sinking fund** invests in securities.
- Instalment = (C - S) × i ÷ [(1 + i)^n - 1]; **no investment in the final year**.
- **Insurance policy method**: endowment premium; maturity certain, return usually lower.

Change in Method or Estimate

- Change in life, residual value or **method** = **change in accounting estimate** (AS 5 / Ind AS 8), applied **prospectively**; no catch-up; disclosed.
- Carrying amount ÷ remaining life: Rs 12,00,000 server after 2 years at Rs 2,00,000, 2 years left = **Rs 4,00,000** a year.

Amortisation of Intangible Assets

AS 26 vs Ind AS 38

Point	AS 26	Ind AS 38
Useful life	Finite; presumed not over 10 years (rebuttable)	Finite or indefinite
Amortisation	SLM unless another pattern clear	Indefinite-life not amortised
Impairment test	On indication; yearly if life over 10 years	Yearly for indefinite-life

- Purchased goodwill (Ind AS 103/36): **not amortised**, yearly impairment; **AS 14** amalgamation goodwill ordinarily **not more than 5 years**.
- Internally generated goodwill **not recognised**; **research expensed**.

Depreciation in Banks

- Scheduled commercial banks follow **AS**: RBI deferred Ind AS on **22 March 2019** until further notice (still so on 30 June 2026).
- **Schedule 10** fixed assets; **Schedule 16** 'Depreciation on bank's property'; **Schedule 2** revaluation surplus; **Schedule 17** policies (board-approved).
- Revaluation reserves count in **CET1 at 55% discount**; **two independent valuers at least once every three years**.
- Co-operative banks: computers **33.33% SLM** (RPCD, **19 January 2006**); UCB software **3 years** (UBD, **24 January 2006**); commercial banks via board policy.
- **s.15(1) BR Act, 1949**: no dividend while intangibles remain, without Central Government exemption.

Most Likely in Exam

- SLM rate = annual depreciation ÷ cost: 90,000 ÷ 5,00,000 = 18%.
- Schedule II: residual up to 5%; laptop 3 years.
- Tax: s.33, block WDV; under 180 days half rate.
- WDV: S 64,000, C 10,00,000, n 3 = 60%.
- Change in method = change in estimate, prospective.
- Revaluation reserve: CET1 at 55% discount.

CHAPTER 7. CAPITAL AND REVENUE EXPENDITURE

Introduction

- **Revenue items** go to Trading and P&L Account; **capital items** to Balance Sheet. Rests on **matching** and **going concern**.

- RBI deferred Ind AS for scheduled commercial banks **"till further notice"** (circular **22 March 2019**), still so on **30 June 2026**; banks follow **AS**.
- Standards (AS / Ind AS): PPE **AS 10 / 16**; intangibles **AS 26 / 38**; grants **AS 12 / 20**; borrowing costs **AS 16 / 23**; impairment **AS 28 / 36**.

Classifying Expenditure

- **Recognition test**: future economic benefits **probable** + cost **measurable reliably** (AS 10; **AS 26 para 20**).
- Tests: purpose (acquire/improve = capital; maintain = revenue), period of benefit, nature of business, materiality.
- Amount and frequency are **only indicators**: Rs 12 lakh overhaul restoring a lift = revenue.

Capital Expenditure

- Benefit **more than one accounting year**; charged via depreciation/amortisation.
- **Cost** = purchase price (less trade discount; **ITC-claimed GST excluded**) + **directly attributable costs** + **dismantling estimate**. Excluded (AS 10, read with **AS 26 para 56**): start-up, launch advertising, training, admin overheads, idle costs, relocation.
- **Qualifying asset** interest capitalised till substantially ready (AS 16 / Ind AS 23); AS 16: ordinarily **12 months**. Costs collect in **CWIP**.
- **Ind AS 16** (Amendment Rules 2022, notified **23 March 2022**, periods on or after **1 April 2022**): excess trial-run proceeds **reduce asset cost** (IFRS: to P&L).
- Robot: **Rs 49.00 lakh** + **Rs 5.70 lakh** = **Rs 54.70 lakh**; training and overheads **Rs 1.60 lakh** expensed. Plant loan Rs 20 crore at 9%: **Rs 1.35 crore** capitalised, **Rs 0.45 crore** expensed.
- Added floor, automation, replacing a major part = capital (old part **derecognised**); whitewashing, AMC, small parts = revenue.

Intangible Assets and R&D

- **Research** always expensed (**AS 26 para 41**); **development** capitalised only if all **six conditions** (**para 44**). Inseparable = research.
- ATM software integral to hardware: part of hardware (**AS 26 para 10**).
- EV R&D: **Rs 9 crore** expensed, **Rs 6 crore** capitalised.
- **Never assets**: internally generated goodwill (**para 35**), brands, mastheads, customer lists (**para 50**).
- AS 26 **para 63**: life presumed **not over 10 years** (rebuttable); Ind AS 38 no cap.

Revenue Expenditure

- Used up **within the year**: carriage inward, salaries, rent, repairs, AMC, depreciation; cloud subscription (no control) generally expensed.

- **Capital**: own installation wages, land stamp duty, pre-use repairs to second-hand machine, freight on machine. **Revenue**: freight on resale goods, training, launch advertising.

Deferred Revenue Expenditure

- Old practice spread **three to five years**; **no longer allowed** (AS 26 para 56 / Ind AS 38; VRS under **AS 15**; no Schedule III head).
- Rs 25 crore launch campaign: **full Rs 25 crore** charged in FY 2025-26.
- Tax: **s.44, Income-tax Act, 2025** (old **s.35D**), from **1 April 2026**: **5 equal instalments**, cap **5% of cost of project** (or capital employed).
- **BR Act s.15(1)**: no bank dividend until capitalised expenses not represented by tangible assets are **completely written off**.

Accounting Entries

- Asset at **net price**; Input GST Dr if ITC available. Installation wages to **Asset A/c**, not Wages. On completion: **Asset A/c Dr, To CWIP A/c**.

Capital and Revenue Receipts

- **Capital receipts**: non-operating, usually non-recurring (capital, loans, asset sales); **revenue receipts**: recurring, raise profit.
- Van cost Rs 12 lakh, dep. Rs 7.20 lakh, sold **Rs 5.70 lakh**: only gain **Rs 0.90 lakh** to P&L (bank: **Schedule 14**).
- **Capital profit**: share premium (Securities Premium), revaluation surplus. **Revenue loss**: stock lost by fire. No shares at discount (**s.53**); **s.123** bars unrealised gains for dividend.

Government Grants

- Recognise on **reasonable assurance** of conditions and receipt.
- **AS 12**: promoters' contribution grant to **Capital Reserve**; asset grant **deducted from cost** or **deferred income**. **Ind AS 20**: **no capital-reserve route**.
- Rs 30 crore line, Rs 10 crore subsidy, 5 years: net charge **Rs 4 crore** a year either way.

Effect of Wrong Classification

An **error of principle**; trial balance still agrees.

Effect of misclassification

Error	Profit (year)	Balance sheet	Next year
Revenue exp. capitalised	Over (less depreciation)	Assets over	Profit under
Capital exp. to revenue	Under (less depreciation due)	Assets under	Profit over
Capital receipt as revenue	Over	Overstated	-
Revenue receipt as capital	Under	Liabilities/capital over	-

- Rs 4 lakh repairs capitalised, 10% SLM: overstated **Rs 3.60 lakh**. Rs 10 lakh chargers to repairs, 15% WDV: year 1 under **Rs 8.50 lakh**, year 2 over **Rs 1.275 lakh**.

Capital and Revenue Items in Banks

- RBI Financial Statements Directions, 2025 (**28 November 2025**); revaluation surplus to **Schedule 2**, not distributable.
- Capital Adequacy Directions, 2025 (**28 November 2025**): revaluation reserves in **CET1 at 55% discount** (**45%** counts); **two independent valuers at least once every three years**.
- **s.17(4) CGST Act**: **50% ITC** option; lapsed half adds to cost. CBS: **Rs 327 lakh**, amortised **Rs 109 lakh** a year.

Bank items in schedules

Item	Nature	Where shown
Premises	Capital	Sch 10: I
ATMs, servers, vehicles	Capital	Sch 10: II
Salaries, repairs, depreciation	Revenue	Sch 16
Interest on advances	Revenue receipt	Sch 13
Commission; asset-sale profit	Revenue / gain	Sch 14

Most Likely in Exam

- Installation wages = capital.
- Research expensed; development needs six conditions.
- Repairs Rs 2 lakh capitalised, 10%: profit over Rs 1.80 lakh.
- AS 12: promoters' contribution to Capital Reserve.
- CET1: 55% discount on revaluation reserve.

CHAPTER 8. BILLS OF EXCHANGE

Introduction

- Buyer's written acknowledgement to pay a **fixed sum on a fixed date**; holder may **discount** it. **NI Act, 1881**.

Negotiable Instruments

- **s.13**: **promissory note, bill of exchange or cheque** payable to order or bearer. Bearer passes by delivery; order by endorsement and delivery.
- **s.118** presumes consideration, date, acceptance before maturity, holder in due course. **Hundis**: custom governs unless excluded (**s.1**).
- **Inland (s.11)** / **foreign (s.12)**; **demand** (no grace) / **usance** (**3 days of grace**); trade / accommodation; clean / documentary. **D/P** with demand, **D/A** with usance bills.
- **RBI Act s.31**: only RBI (or Central Government where allowed) may issue a bill, hundi or PN **payable to bearer on demand** (cheques, drafts excluded); bearer PN only by RBI or Central Government.

Bill of Exchange

s.5: writing containing an **unconditional order**, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to bearer.

- Essentials: writing; **order**, not request; unconditional; signed; drawee, sum, payee **certain**; **money only**; time bill **stamped** (**Indian Stamp Act, 1899**).
- Parties (**s.7**): drawer, drawee/acceptor, payee, **holder (s.8)**, endorser, drawee in case of need, acceptor for honour. **Three capacities**, not necessarily three persons.
- Only **bills** are accepted. Drawee may ask **48 hours** (excluding public holidays) (**s.63**). **Qualified acceptance (s.86)** may be treated as dishonour; taken without consent, earlier parties are discharged.
- **Endorsement (s.15)**: blank (bearer), full, restrictive, **sans recours** (not liable), facultative, **partial** (invalid).
- **Holder in due course (s.9)**: for consideration, before payable, no reason to suspect defect. Dishonour: **s.91** non-acceptance, **s.92** non-payment.

Promissory Note and Cheque

- **PN (s.4)**: unconditional **undertaking** by maker; two parties; never accepted; 3 days of grace if timed; private PN must name payee (**RBI Act s.31(2)**). **DPN** is a loan document.
- PN maker **primarily** liable; bill drawer **secondarily**. A foreign bill may be drawn in sets; a PN cannot.

- **Cheque (s.6)**: bill on a specified banker, payable on demand; includes truncated and electronic cheques.
- **CTS** continuous clearing since **4 October 2025**; Phase 2 deferred. Validity **3 months** (from **1 April 2012**; earlier six).

Section 138 Limits

Step	Limit	Basis
Demand notice	Within **30 days** of learning of return	s.138
Drawer pays	Within **15 days** of notice	s.138
Complaint	Within **one month** after the 15 days	s.138
Punishment	Up to **2 years**, fine up to **twice** amount, or both	s.138
Interim compensation	Up to **20%** of cheque amount	s.143A (2018)
Appeal deposit	At least **20%** of fine or compensation	s.148

Due Date of a Bill

- **s.22**: third day after the day expressed; no grace for demand, sight or on-presentment. **s.23**: no corresponding day, **last day of month**. **s.24**: exclude day of date or sight.
- **s.25**: public holiday (incl. **Sundays**) → **next preceding business day**; emergency holiday → next business day (**textbook convention**).
- Due date = Date (or acceptance, after sight) + term + 3 days.

Worked Due Dates

Bill	Due date	Rule
10 Nov 2025, 2 months after date	**13 Jan 2026**	s.23 + 3 days
Same, after sight; accepted 17 Nov	**20 Jan 2026**	From acceptance
31 Oct 2025, 1 month	**3 Dec 2025**	Last day of month
60 days after sight; accepted 8 Jan 2026	**12 Mar 2026**	s.24
12 Jul 2025, 1 month	**14 Aug 2025**	15 Aug holiday
4 Oct 2025, 2 months	**6 Dec 2025**	7 Dec Sunday
1 Dec 2025, 90 days after date	**4 Mar 2026**	90th day 1 Mar + 3

Accounting for Bills

- Drawer: **Bills Receivable Dr To Drawee**; drawee: **Drawer Dr To Bills Payable**. Drawee passes **no entry** when drawer discounts, endorses or collects.
- Discount = Face value × Rate × Days ÷ 365. Rs 2,00,000, **9%, 72 days**: **Rs 3,551**; net **Rs 1,96,449**.
- Unmatured discounted bill: **contingent liability** (**AS 29**, Schedule III); **Ind AS 109**: with recourse, usually receivable plus borrowing.

Dishonour, Noting and Protest

- Notice (**s.93**) to every party to be held liable, else **discharged**; exceptions **s.98**.
- **Noting (s.99)**, **protest (s.100)** by notary; optional for inland bills; foreign bills if law of place of drawing requires (**s.104**). Charges finally borne by **acceptor**.
- Rs 2,00,000 discounted bill dishonoured, noting Rs 500: **Drawee Dr 2,00,500 To Bank**; discount **not reversed**.

Retirement, Renewal and Insolvency

- Rebate = Amount × Rate × Unexpired period: Rs 2,00,000, 12%, 1 month = **Rs 2,000**. **Expense for drawer, income for acceptor**.
- Renewal: Rs 1,50,000 less Rs 50,000 paid + interest **Rs 2,000** = new bill **Rs 1,02,000**.
- Insolvency: Rs 80,200 at **40 paise** gives **Rs 32,080**; bad debt **Rs 48,120**; acceptor credits **Deficiency A/c**.

Accommodation Bills

- No sale behind it; accommodation party liable to a **holder for value**. Chains: **kite flying**. Banks **must not finance** them.
- **Discount shared in ratio of proceeds**: Rs 1,20,000, 3 months, 12% = **Rs 3,600**; each bears **Rs 1,800**.
- Insolvency: claim = net balance (Manoj owes **Rs 1,10,000**; bad debt **Rs 55,000**).

Bill Books

- **B/R Book** total **debited** to Bills Receivable A/c; **B/P Book** total **credited** to Bills Payable A/c (records **date of acceptance**).

Banks and Bills

How Banks Handle Bills

Facility	Bill type	Bank's role
Bills purchased	Demand, usually D/P	Pays at once
Bills discounted	Usance, often D/A	Face value less discount
Collection	Any bill	Agent; commission
LC bills negotiated	Under LC	Claims from LC-opening bank

- **RBI (Commercial Banks - Credit Facilities) Directions, 2025** (issued **28 November 2025**): Board-approved policy. Overdue: demand bill unpaid after transit plus grace period; usance bill unpaid on due date.
- Genuine trade only; rediscount only **usance bills**. **NPA**: overdue **more than 90 days**.
- Unexpired discount = **rebate on bills discounted** (liability): Rs 5,00,000, 7.3%, 73 days: **Rs 7,300**; rebate on 31 Mar 2026 **Rs 3,000**; FY 2025-26 income **Rs 4,300**.
- **TReDS**: MSME receivables, **without recourse**; widened **7 June 2023** (insurers, factoring entities, secondary market).

Most Likely in Exam

- Due date = date + term + 3 days; holiday: preceding business day (s.25).
- No grace for demand or sight bills.
- Discounted bill dishonoured: Drawee Dr To Bank; discount not reversed.
- Accommodation discount shared in ratio of proceeds.
- Overdue more than 90 days: NPA.

CHAPTER 9. OPERATIONAL ASPECTS OF ACCOUNTING ENTRIES

Introduction

- **s.29, BR Act 1949**: accounts in **Form A** (Balance Sheet) and **Form B** (P&L), **Third Schedule**; presentation per RBI (Commercial Banks – Financial Statements: Presentation and Disclosures) Directions, 2025, issued **28 November 2025**.
- Deposit = bank's **liability**; loan = **asset**. Debits always equal credits.
- **CBS** updates ledger, day book and GL instantly; it ends manual posting, **not vouchers** (system entries get transaction ID and audit trail).

Peculiar Features of Bank Accounting

- **Voucher posting system**: customer ledger posted **first**, day book (branch **journal**) later, totals to **GL**.
- GL **control account** balance = total of its **subsidiary ledger**.
- **Banking Companies (Period of Preservation of Records) Rules, 1985**: ledgers, scrolls, paid cheques, pay-in-slips, most vouchers at least **8 years**; some registers **5 years**. KYC/PMLA records **5 years** after relationship or transaction ends.
- Day book, **GL trial balance** and cash closed **daily**; inter-branch items via Branch Adjustment/HO account.

Types of Transactions

- **Three streams**: **cash**, **transfer**, **clearing** (via **CTS**), each with its own scroll. Cash leg always Cash Account; clearing leg a Clearing/Settlement account.
- **Outward clearing**: other banks' cheques lodged by our customers; **inward**: our customers' cheques presented by other banks.
- Bulk interest credit = transfer entry; NEFT/RTGS/IMPS/UPI act as transfers via settlement accounts.

Vouchers in Bank Transactions

- Types: **debit, credit, composite**; **consolidated** voucher covers many accounts with an attached list.
- **Composite**: both legs on one form (bills for collection, LCs/guarantees, rectification).
- Cash remittance **below Rs 50,000**: application is the credit voucher. Challans: e-Pay Tax, GST **CPIN**, PPF.
- Rs **200** fee + **18%** GST on **2,000** accounts: debit **Rs 4,72,000** = income **Rs 4,00,000** + GST **Rs 72,000**.
- Voucher shows amount in **figures and words**, narration, maker and checker. CBS: **transaction ID = voucher number**.

Checking, Balancing and Day-End

- **Balancing of books**: sub-ledgers vs GL control. Difference **divisible by 9** suggests **transposition** (Rs 5,400 as Rs 4,500: **Rs 900**).
- **EOD** run: interest, standing instructions, charges, system NPA marking, trial balance, **daily** sub-ledger vs GL tally; **BOD** opens next day.
- Closing cash = Opening + Receipts - Payments: 18,40,000 + 9,65,000 - 12,10,000 = **Rs 15,95,000**.

Accounting Systems of Different Banks

- Systems differ (hardware, software, security, volume); **principles stay the same**.

- CBS: central database, parameterised GL heads, maker-checker, **audit trail** (cannot be erased), settlement accounts **reconciled daily**.

Entries for Deposit Accounts

- **SB interest** (RBI (Commercial Banks – Interest Rate on Deposits) Directions, 2025, **28 November 2025**): **daily balance**, credited **quarterly or shorter**. Interest = Sum of daily balances × Rate ÷ 365; **Rs 68,40,000** at **2.75%** = **Rs 515**.
- Cost head: **Interest Paid on Deposits** (Schedule 15, Form B); TD interest accrued quarterly to Interest Payable.

TDS on Deposit Interest

Item	Position (from 1 April 2026)
Section	**s.393(1)**, Income-tax Act, 2025 (old **s.194A**)
Rate / limit	**10%**; nil up to **Rs 50,000** (senior **Rs 1,00,000**)
Declaration	**Form 121** replaces **15G/15H** from tax year 2026-27
Timing	Credit or payment, **whichever is earlier**; 31 March accrual included

- Rs **8,00,000** TD at **7.2%** compounded quarterly: interest Rs 59,173.95, TDS **Rs 5,917**, maturity **Rs 8,53,257**.

Entries for Loans and Advances

- Interest on **daily debit balance** at **monthly rests**: Dr loan; Cr Interest Earned. CC Rs 10 lakh at **10.5%**: June interest **Rs 6,242**.
- **NPA**: overdue **more than 90 days**; CC/OD **out of order for 90 days** (RBI (Commercial Banks – Income Recognition, Asset Classification and Provisioning) Directions, 2025, **28 November 2025**); system marking.
- NPA income only on **receipt**; unrealised interest **reversed** (Dr Interest Earned; Cr **Interest Suspense**).

Clearing and Digital Payment Entries

CTS and Payment Systems

System	Position	Date
CTS revised	**9 am–3 pm** present, **9 am–7 pm** confirm	Circular **24 Dec 2025**
CTS Phase 1	Continuous clearing; 10 am–4 pm present, 10 am–7 pm confirm	From **4 Oct 2025** (circular 13 Aug 2025)
CTS Phase 2	**Three-hour** response; deferred until further notice	Was due **3 Jan 2026**
NEFT	24x7, **48 half-hourly** batches	**16 Dec 2019**
RTGS	24x7, **Rs 2 lakh** and above	**14 Dec 2020**

- Unconfirmed cheque treated as **approved**. Outward: Dr Clearing Settlement; Cr customer. Inward: Dr drawer; Cr Clearing Settlement.
- Uncreditable inward NEFT/RTGS: **Inward Parking (Sundry)** account, then returned. UPI/IMPS/ATM cleared by **NPCI**.

Remittances, Contra Entries and Charges

- DD: Cr **Drafts Payable/Branch Adjustment**. Rs 2,50,000 at **0.10%**: commission **Rs 250**, GST **Rs 45**, debit **Rs 2,50,295**.
- Remittance **Rs 50,000 or more**: only by account debit or cheque, **never cash**.
- **Contra entries** for bills, LCs, guarantees; LCs/guarantees = **Contingent Liabilities (Schedule 12)**; bills for collection at foot of Form A.
- Guarantee **Rs 25,00,000** at **1.5% p.a.**: commission **Rs 37,500** + GST **Rs 6,750**. Errors fixed by **composite voucher**.

Comprehensive Illustration

- Riya's SB: **Rs 24,500** + 26,000 - 37,459 = **Rs 13,041**; GL totals **Rs 63,459** each; SB control head falls **Rs 11,459**.

Most Likely in Exam

- Voucher posting system: ledger first, day book later.
- Own customer's cheque from another bank = inward clearing.
- Composite voucher: both legs; consolidated: many accounts.
- TDS s.393(1), 10%; limit Rs 50,000 (seniors Rs 1,00,000); Form 121.
- NPA: overdue more than 90 days; unrealised interest reversed.
- Charges and commission attract 18% GST.

CHAPTER 10. BACK OFFICE FUNCTIONS AND HANDLING UNRECONCILED ENTRIES IN BANKS

Introduction: Back Office Layers

- **Front office** earns revenue; **middle office** monitors risk and limits; **back office** processes, confirms, settles, accounts for and reconciles.
- Back office independent of front office (**segregation of duties**); every entry under **maker-checker**.
- CBS enabled **CPCs**: **RACPCs**, KYC hubs, **CTS clearing hubs**, trade finance CPCs, treasury back office.

Functions of the Back Office

- Covers bookkeeping, deposits, loans, compliance, digital banking and payments.
- **Clearing hub** matches CTS settlement with cheques presented and received; gap = **clearing difference**.
- **Treasury back office** confirms deals, not the dealer: SWIFT **MT300** (forex), **MT320** (money market), CCIL **NDS-OM**, **FX-CLEAR**. G-secs settle via CCIL on **DvP** in the **SGL account on e-Kuber**; forex via nostros.
- **Trade finance CPC**: LCs, bills, guarantees, FEMA reporting.

Reconciliation Function: Overview

- Comparing two records of the same transactions and explaining every difference; old unreconciled entries are where **frauds most often hide**.
- Five areas: **digital payments/intermediaries**, **correspondent banks**, **RBI and other banks**, **intra-branch**, **inter-branch**.

Intermediaries and Digital Payments

- **Payment aggregators**: Master Direction dated **15 Sep 2025**; **PA-P, PA-O, PA-CB**. Non-bank PA net worth **Rs 15 crore** on applying, **Rs 25 crore** by end of **third** FY after authorisation; banks need no separate authorisation. Escrow with an **SCB** (one more allowed); **quarterly** certificates.
- **ATM three-way reconciliation**: **EJ**, **switch**, **CBS** (+ **NPCI NFS** report for other banks' cards). Example: loaded **Rs 20,00,000**, EJ **Rs 14,35,000**, switch **Rs 14,40,000**: **Rs 5,000** failed dispense; reversed 3 days late = **Rs 300**.
- **NEFT** 24x7 from **16 Dec 2019**; **RTGS** 24x7 from **14 Dec 2020**. UPI, IMPS, NFS, NACH run by **NPCI**.
- RBI circular **20 Sep 2019** (effective **15 Oct 2019**): **Rs 100 per day** compensation for delay, paid without a complaint.
- From **1 Oct 2021**: **Rs 10,000 per ATM** if out of cash **more than 10 hours** in a month.

TAT for failed transactions

Channel	Failure	Reverse by
ATM / micro-ATM	Cash not dispensed	**T+5**
Card to card	Card not credited	**T+1**
POS (card present)	No charge slip	**T+5**
IMPS / UPI transfer	Beneficiary not credited	**T+1**
UPI merchant payment	No merchant confirmation	**T+5**
NACH	Delay in credit	**T+1**

Correspondent Banks: Nostro and Vostro

- **Nostro**: our account with you (foreign currency); **vostro**: your account with us (rupees); **loro**: a third bank's; **mirror**: bank's own record of its nostro.
- Statements via SWIFT **MT940/MT950**. Example: mirror **USD 250,000**, statement **USD 278,000**; reconciled **USD 279,500**.
- RBI circulars **1 Jul 1999**, **24 Aug 2001**, revised **11 May 2009**. One-off (May 2009): credits **below USD 2,500** originating up to **31 Mar 2002** to P&L, appropriated to **General Reserve**.

Accounts with RBI and Other Banks

- **RBI current account** on **e-Kuber** (CRR, LAF, MSF, settlements, currency chests), reconciled **daily**. **SDF** is the LAF floor from **8 Apr 2022**.
- Investment Portfolio Directions, 2025 (**28 Nov 2025**): G-secs reconciled with **PDO** records **at least monthly**; investment book **at least quarterly**.
- **Clearing differences**: **July 2003** one-time netting of entries **below Rs 500** over **three years** old; net debit to P&L, net credit to Blocked Account; **100% check** by auditors.

Intra-branch Reconciliation

- **Balancing**: GL control head = subsidiary total. Example: GL exceeds customers by **Rs 45,000** (pending NEFT credit); report, never force.
- **Suspense** = temporary **debits** (asset): agency warrants, shortages, frauds; favourite place to hide fraud. **Sundry deposits** = temporary **credits** (liability).
- **DEA Fund** (**s.26A BR Act**; Scheme **2014**): credits unclaimed or inoperative **10 years or more** (DDs, sundry, NEFT, ATM) move on **last working day of the next month**; claims still paid.

Reconciliation of Inter-branch Entries

- **Originating** entry meets a **responding** entry; matched pairs drop out.
- Net credit: **Schedule 5**, item **II**; net debit: **Schedule 11**, item **I**; never borrowings.

- DD example: Pune debits customer **Rs 75,177** (Rs 75,000 + commission **Rs 150** + GST **Rs 27**). A forged DD of **Rs 2,40,000** leaves an **unmatched debit**, the classic fraud sign.
- **Pointing accounts**: mandatory reference, auto-matched; **non-pointing**: manual review. **Forced matching** is the most serious error.

RBI Norms on Inter-branch Entries

- Commercial Banks - Financial Statements: Presentation and Disclosures Directions, 2025 (**28 Nov 2025**).
- Objectionable: disguising cash, **window dressing**, dummy entries hiding overdue loans, netting liabilities against assets.
- Category-wise accounts; **DD entries kept apart**. Example: net debits **Rs 2,50,000 + Rs 60,000 = Rs 3,10,000** provision; net credit ignored.

RBI limits for unreconciled entries

Account	Trigger	Treatment
Inter-branch credits	Over **5 years**	Blocked Account; excluded from netting; CRR/SLR
Blocked Account adjustment	Over **Rs 1 lakh**	Two officials, one outside branch (preferably Controlling/HO)
Inter-branch net debit	Over **6 months**	**100%** provision; no cross set-off
Nostro debits	Over **2 years** (from 1 Apr 2002)	**100%** provision
Nostro credits	Over **3 years**	Blocked Account; CRR/SLR
Unclaimed credits	**10 years** or more	DEA Fund

Reconciliation Set-up in Banks

- **Central Reconciliation Department** at HO works on CBS exception reports.
- Branches send **daily statements**, including **NIL statements**.
- **A-B-C analysis** (high-value first); scrutinise **reversals**; Board/Audit Committee oversight; auditors report in the **LFAR**.

Most Likely in Exam

- Inter-branch credits over **5 years**: Blocked Account.
- Over **6 months**: **100%** provision on category-wise net debits.
- Nostro debits over **2 years**: 100% provision.
- Failed ATM: **T+5**; UPI/IMPS: **T+1**; **Rs 100 per day**.
- Net debit of inter-office adjustments: **Schedule 11**.
- Unclaimed **10 years** or more: DEA Fund.

CHAPTER 11. BANK AUDIT AND INSPECTION

Introduction

Audit: independent, systematic examination of books and systems to opine on a **true and fair view**; gives only **reasonable assurance**.

- **Inspection**: operations and compliance (own I&A Dept; RBI under **s.35 BR Act**). **Investigation**: occasional, issue-specific (e.g. suspected fraud).
- Companies Act **Chapter X (ss.139-148)** applies subject to **BR Act s.30**. Also **s.41 SBI Act**, **s.19 RRB Act**, s.10 Acquisition Acts.
- **s.139** (listed company): individual max **one term of 5 years**, firm max **two terms of 5 consecutive years**. **s.143(12)**: fraud of **Rs 1 crore or more** to Central Government. **s.144**: no non-audit services.

The Audit System of a Bank

- **Three lines of defence**: business units, risk and compliance, internal audit.
- **SA 610**: statutory auditor may use internal auditors' work but alone stays responsible.

Risk-Based Internal Audit (RBIA)

- Audits **management of risk**. Guidance Note **27 Dec 2002**; circular **7 Jan 2021** (effective immediately) prevails.
- Units rated on **business risk** and **control risk**; matrix sets frequency in ACB-approved plan. High + medium = **Very high**; high + high = **Extremely high**.
- HIA tenure **preferably not less than 3 years**; no business targets; internal audit **cannot be outsourced**; ACB meets HIA **at least once a quarter**.
- Extended (**3 Feb 2021**) to deposit-taking NBFCs, other NBFCs **Rs 5,000 crore+**, UCBs **Rs 500 crore+**, by **31 Mar 2022**.

Concurrent Audit

- Examines transactions as they happen or very soon after; **early warning system**; stops **revenue leakage**. Circular **18 Sep 2019** (replaced 16 Jul 2015).
- Own officers or external auditors; retired staff up to **age 70**. Scope by **HIA with prior ACB approval**; all **CPCs** covered.
- External auditor generally **not more than 5 years**; same branch **max 3 years**. ACB reviews findings **quarterly**, system **annually**.

Information Systems Audit and CAATs

- Guidelines **29 Apr 2011** now in **IT Governance MD**, issued **7 Nov 2023**, effective **1 Apr 2024**.

- IS Audit Policy approved by ACB, reviewed **at least once a year**; **DR drills at least half-yearly**; **SIA 520** for IT environment.
- **CAATs** audit 'through the computer'.

Statutory Audit

- BR Act **s.29** Forms A and B; **s.30(1A)** RBI **prior approval** for auditor; **s.30(1B)** special audit at bank's cost; **s.31** publish within **3 months**; RBI may extend by up to **3 more months**.
- Focus: **IRAC**, investments, CRR, SLR, CRAR. Branch audit **s.143(8)**; SAs under **s.143(10)**.
- **LFAR** (**5 Sep 2020**, from **FY 2020-21**): Annex **I** SCAs, **II** branch, **III** large, irregular and critical accounts; to RBI within **60 days** of submission.
- Tax audit: FY 2025-26 **s.44AB** (3CA/3CD); tax years beginning on or after **1 Apr 2026**: **s.63, Income-tax Act, 2025**, **Form 26**.

Appointment of Statutory Auditors

- Guidelines **27 Apr 2021**. PSBs use **C&AG** list; others shortlist **at least 2 firms per vacancy**; RBI application **before 31 July**.
- Assets **Rs 15,000 crore or more**: **joint audit**. Tenure **3 continuous years**; cooling **6 years**.
- Firm max **4 commercial banks** (not more than one PSB), **8 UCBs**, **8 NBFCs**. Concurrent auditor cannot be SCA; **one-year gap** after non-audit work.
- SCAs cover **top 20 branches**, at least **15% of gross advances**. Lapses reported to RBI within **two months** of completing the audit.
- Banking Laws (Amendment) Act, 2025 (in force **1 Aug 2025**): PSBs pay their statutory auditors themselves.

Maximum number of SCAs

Asset size	Max SCAs
Up to Rs 5 lakh crore	**4**
Above Rs 5 to 10 lakh crore	**6**
Above Rs 10 to 20 lakh crore	**8**
Above Rs 20 lakh crore	**12**

Other Audits in Banks

- **Revenue audit**: penal charges issued **18 Aug 2023**; applied to fresh loans from **1 Apr 2024**, existing loans at next review, not later than **30 Jun 2024**.
- **Stock audit**: recomputes **drawing power**; DP 75% × 400 + 60% × 200 = **Rs 420 lakh**.
- **Credit audit / LRM** (RBI 1999 guidance); **management audit** reviews use of resources.

- **GST**: CA audit removed from **1 Aug 2021**; turnover above **Rs 5 crore** files GSTR-9 with self-certified **GSTR-9C**.

Fraud MD time limits (15 Jul 2024)

Event	Time limit
RFA **Rs 3 crore+** to CRILC	**7 days**
Decide fraud or remove flag	Ordinarily **180 days**
Show-cause reply	At least **21 days**
Fraud Monitoring Return	**14 days** of classification

RBI Inspection and Supervision

- **BFS November 1994**; off-site surveillance **1995**. **CAMELS** (Indian), **CALCS** (foreign).
- **SPARC** from cycle beginning **April 2013**; unified **Department of Supervision 1 Nov 2019**.
- RBI inspects any bank at any time under **s.35 BR Act**; must if Central Government directs.
- **PCA**: issued **2 Nov 2021**, effective **1 Jan 2022**; tracks capital (CRAR/CET1), asset quality (net NPA), leverage (Tier 1 leverage); **three risk thresholds**.

Compliance Function and Audit Committee

- **CCO** (**11 Sep 2020**): tenure **at least 3 years**; age **not more than 55**; **15 years** in banking/financial services, **5** in audit, finance, compliance, legal or risk; no business targets.
- **ACB** (Governance Directions, **28 Nov 2025**): **only non-executive directors**; Board Chair cannot be member; **independent director** chairs; meets **at least once a quarter**; quorum **3**, **two-thirds** of those present independent.

Most Likely in Exam

- s.30(1A): RBI prior approval for auditors.
- Internal audit cannot be outsourced.
- SCAs 4/6/8/12; 3-year tenure, 6-year cooling.
- LFAR Annex III: large, irregular and critical accounts.
- IT MD effective 1 Apr 2024.
- CCO age not more than 55.

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