

Introduction to Accounting

Introduction

The history of accounting is as old as civilization. Accounting was present in one or the other form since ancient times. But the modern system of accounting owes its development to Luca Pacioli who wrote a book on Mathematics called 'Summa'. A portion of this book contains knowledge of business and book keeping. In fact, this book is considered as the first book on double entry system of book-keeping. Later on, Accounting developed with the contributions of many individuals and institutions.

1.1 Meaning of Accounting

1. Define accounting (or) Give the meaning of accounting.

1/2 Marks

Ans: According to **American Institute of Certified Public Accountants (AICPA)**, "Accounting is the art of recording, classifying and summarising in a significant manner and in terms of money, transactions and events which are in part at least of a financial character and interpreting the results thereof". Or

According to **American Accounting Association (AAA)** "Accounting is the process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users of information" Or

Accounting is the process of identifying, measuring, recording and communicating the required information relating to the economic events of an organization to the interested users of such information.

2. Expand AICPA.

1 Mark

Ans: AICPA: **American Institute of Certified Public Accountants.**

3. What is accountancy?

1 Mark

Ans: According to Eric Kohler "Accountancy is the theory and practice of accounting".

1.2 Accounting as a Source of Information

4. State any two internal users of accounting information.

2 Marks

Ans: (1) Chief Executive (2) Financial Officer (3) Vice President

5. State any two external users of accounting information?

2 Marks

Ans: (1) Investors (2) Creditors (Bank, Debenture holders and others Lenders)

(3) Tax authorities (4) Stock exchanges (5) Customers (Write any two)

6. State any two users of accounting information.

2 Marks

Ans: (1) Management

(2) Creditors

(3) Investors

(4) Tax authority

7. State any two branches of accounting

- Ans: (1) Financial Accounting
(2) Cost Accounting
(3) Management Accounting

2 Marks

8. State any two qualitative characteristics of accounting information.

- Ans: (1) Reliability (2) Relevance
(3) Understandability (4) Comparability (Any two)

2 Marks

1.3 Objectives of Accounting

9. State any two objectives of accounting

- Ans: (1) Maintenance of records of business transactions.
(2) Calculation of profit and loss
(3) Depiction of financial position
(4) Providing accounting information to its users (Any two)

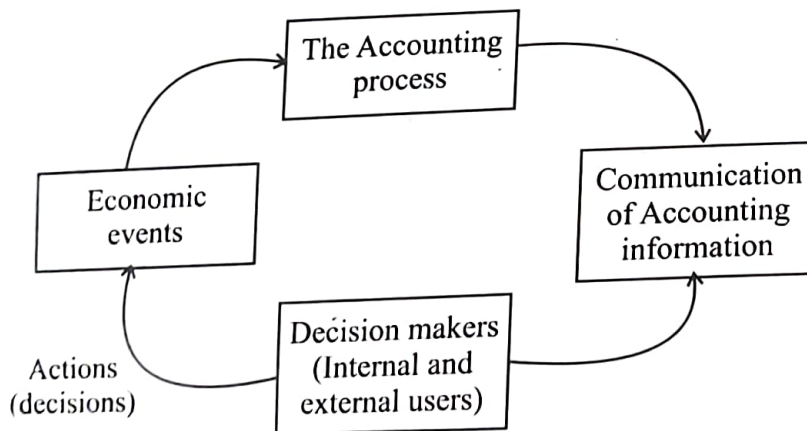
2 Marks

Practical oriented question:-

10. Draw a diagram of accounting process

5 Marks

Ans:



1.4 Role of Accounting

Accounting is regarded as a language of business. It collects and communicates economic information about an enterprise to a wide variety of interested parties.

1.5 Basic Terms in Accounting

11. What is Entity?

1/2 Marks

Ans: Entity means a reality (i.e., a thing or a person) having a definite individual existence. Business entity means a specifically identifiable business enterprise like Big bazaar, ITC Ltd etc.,

12. What is a transaction?

1/2 Marks

Ans: A transaction means an event, activity or dealing involving the exchange of money or money's worth between the persons (or business firms)

- E.g: (a) Purchase of goods for Rs. 10,000
(b) Salary paid to salesman Rs. 4,000

13. State two types of transactions.

2 Marks

Ans: (1) cash transaction
(2) Credit transaction

14. What are credit transactions? Give an example.

2 Marks

Ans: Credit transactions are those transactions in which receipt or payment of cash is postponed to a future date e.g. goods purchased from Mr. Anand on credit for Rs. 1000.

15. What are cash transactions? Give an example.

2 Marks

Ans: Cash transaction is a transaction which involves immediate receipt and payment of cash e.g. Goods sold for cash Rs. 1,000.

16. What are Assets?

2 Marks

Ans: Assets are economic resources of an enterprise. They are used by the business in its operations. Assets include:

- (a) Fixed assets such as land, building, machinery, furniture etc. (2 examples 2 marks)
- (b) Current assets such as stock of goods, cash etc.

17. State any two types of assets.

2 Marks

Ans: (1) Fixed Assets e.g., Machinery
(2) Current Assets e.g., Cash

18. What are Fixed Assets?

2 Marks

Ans: Fixed assets are assets held on a longterm basis. These assets are used for normal operations of the business.
E.g. land, building, machinery, furniture etc.

19. What are current assets?

2 Marks

Ans: Current assets are assets held on a short term basis.
E.g. Debtors, bills receivable, stock, cash etc.

20. What are Liabilities?

2 Marks

Ans: Liabilities are obligations or debts that an enterprise has to pay. In other words, liabilities are the amounts due from a business to outsiders. Examples: Creditors, Bank loan.

21. What are long term liabilities?

2 Marks

Ans: Long term liabilities are those that are usually payable after a period of one year. E.g., Long term loan, Debentures.

22. What are short term liabilities?

2 Marks

Ans: Short term liabilities are obligations that are payable within a period of one year. E.g. Creditors, bills payable, bank overdraft.

23. State any two examples of short term liabilities.

2 Marks

Ans: (1) Creditors
(2) Bills payable
(3) Bank overdraft (any two)

24. What is capital?

1/2 Marks

Ans: Capital is the amount invested by the owner in the business. (or) capital = Assets – Liabilities

25. Give the meaning of voucher?

1/2 Marks

Ans: The documentary evidence in support of a transaction is known as voucher. Examples: Cash memo, receipt, etc.

26. Give an example of voucher.

- Ans: (1) Cash memo
(2) Invoice
(3) Receipt (any one)

1 Mark

27. What are goods?

Ans: Goods refer to the products in which a trader deals. Example: for a stationery merchant, stationery articles like books, pens, pencils, ink, paper etc. are his goods.

2 Marks

28. What are drawings?

Ans: Drawings refer to cash, goods or other assets withdrawn (i.e., taken away) by the owner from business for personal use.

2 Marks

29. Give the meaning of stock.

Ans: Stock (or inventory) means the value of unsold goods or unused materials in a concern at any particular point of time.

2 Marks

The value of stock at the end of the year is called closing stock. The value of stock in the beginning of the year is called opening stock.

30. Who are debtors?

Ans: Debtors are persons or other entities who owe money to the business for buying goods and services on credit. Debtors are asset to the business.

1/2 Marks

31. Who are creditors?

Ans: Creditors are the persons or other entities to whom the business owes money for providing the goods or services on credit. Creditors are liabilities to the business.

1/2 Marks

Other Basic Terms in Accounting

(a) **Sales:** Sales are total revenues from goods sold or services provided. Sales may be cash sales or credit sales.

(b) **Revenue:** Revenue or income means the earnings of a business from the sale of goods or from rendering of services to the customers.

(1 Mark)

Example: Sales revenue, commission received, rent received, interest received etc. (2 examples 2 marks)

(c) **Expenses:** Costs incurred by a business in the process of earning revenue are known as expenses. It is expired cost.

Examples: Cost of goods sold, salary paid, rent paid, interest paid. (2 examples 2 marks)

(d) **Expenditure:** Spending money or incurring a liability for some benefit, services or property received is called expenditure.

- Examples:* Payment of rent
Payment of salary
Purchase of goods
Purchase of machinery
Purchase of furniture

If the benefit of expenditure is exhausted within a year, it is treated as an expense. (revenue expenditure)

Examples: Payment of rent
Payment of salary (2 examples 2 marks)

If the benefit of an expenditure lasts for more than a year, it is treated as an asset (Capital expenditure)

Examples: Purchase of machinery

(2 examples 2 marks)

Purchase of Furniture

(e) **Profit:** The excess of revenue over expenses during an accounting year is profit. Profit increases the owners' equity. i.e., Profit = Revenue – Expenses.

(f) **Gain:** A profit that arises from events or transactions which are not regular but incidental to business is known as gain. (1/2 Mark)

Examples: Profit on sale of fixed assets.

Winning a court case

(g) **Loss:** The excess of expenses of a period over its related revenues is termed as loss. It also refers to money or money's worth lost without receiving any benefit in return. (1/2 Mark)

Examples: Loss of goods by fire.

Loss of cash by theft.

(h) **Purchases:** Purchases are total amount of goods procured by a business for production or sale. (1/2 Mark)

(i) **Discount:** - Discount is the deduction in the price of the goods sold. It is offered in two ways:

(1) Trade discount

(2) Cash discount

(1) **Trade discount:** - Deduction of agreed percentage (say 5%) of list price offered at the time of sale of goods is known as trade discount. It is generally offered by manufacturers to wholesalers and by wholesalers to retailers. (1/2 Mark)
It does not appear in the books of accounts.

(2) **Cash discount:** - Cash discount is certain deduction given to debtors in amount due in case if they pay the amount within the stipulated period. This deduction is given at the time of payment on the amount payable. It should be entered in the books of both the debtors and creditors. (1/2 Mark)