UNIT IV

I ~~So~~ CONCEPTS & CONVENTIONS

Accounting principles or rules or concepts are general guidelines for sound accounting practices. These are known as "GAAP" – General Accepted Accounting principles. GAAP have a set of rules and guidelines used in preparing Financial Accounting reports. A list of Accounting Concepts are:–

① BUSINESS ENTITY CONCEPT: According to this concept, business is treated as a separate entity, which is distinct from its owners. All the transactions of the business is recorded from the business point of view. Even the proprietor is treated as a creditor to the extent of his capital. It is deemed that the Proprietor has given money and the business has received money. The personal transactions of the proprietor will not be recorded in the books of accounts.

② DUAL ASPECT CONCEPT: This is the basic principle of accounting. According to this concept, every transaction has a dual aspect, i.e. two fold effect. The receiving and giving aspects are the two aspects of every business transaction. This principle is called double entry system of book keeping. As per dual aspect, total assets ~~& total~~ is equal to Total liabilities. This equation is called Accounting equation.

Liabilities = Assets

(or)

Capital - liabilities = Assets

(or)

Capital = Assets - liabilities

3) GOING CONCERN CONCEPT: This concept assumes that the business will continue forever and will not be liquidated in the near future. The Assets are recorded at the cost of its acquisition but not at market values. Because market values are useful only in the event of liquidation. If this assumption is not made, the business is going to be liquidated, the accountant has to spend alot of time in finding out the market price for disposal of asset.

4) ACCOUNTING PERIOD CONCEPT :- If we go on recording the transactions in account books, the business cannot determine income. At one point or interval, the accounts should close. Accountants generally adopts twelve Month period for ~~adopting~~ Measuring the income of a concern. This time interval is called "Accounting period".

(5) MONEY MEASUREMENT CONCEPT: This Concept signifies that in accounting a record is made only of those transactions or events which can be expressed in terms of money. Non Monetary events such as retirement of a manager, Working conditions of workers etc. Cannot be recorded in accounting books. This Concept express all heterogeneous items [such as Bank balance, stock, Furniture, machinery, buildings etc.] in terms of a common denominator that is money].

(6) COST CONCEPT: According to this concept, an asset is recorded in the books at the price paid to acquire it and this cost is the basis for subsequent accounting years for
the asset.

The asset recorded at cost price at the time of purchases are systematically reduced by the process of depreciation. These assets disappear from Balancesheet when their economic life is over and they will ~~be~~ ~~depre~~ be depreciated and sold as scrap

⑦ MATCHING CONCEPT: Matching concept states that the expenses of a given period must be related to the revenues of that particular period only. ~~The revenues earned for the period~~ only. The revenues earned for the period must be determined first and then the expenses are to be matched to the revenues earned during that given period.

⑧ REALISATION/ACCRUAL CONCEPT: Revenue is said recognised only when the sale is made, not when the sale proceeds are collected. In other words, accountant does not recognise revenue until it is considered to have been realised. It is necessary that the revenue is to be recognised before cash is received.

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5) Accounting Conventions refers to customs, traditions, usage or practices followed by accountants as a guide in preparation of financial statements. They are followed to make the financial statement clear and Meaningful.

① Convention of consistency:- the Accounting practices from one accounting period to another Accounting period should not change. The comparision of one accounting period with that in past is possible only when the concept of consistency is followed. This concept play its role when alternative accounting method is equally acceptable. For example:- Fixed asset is depreciated over its useful life of a asset. The method of a calculating will be same for calculating depreciation, there are several methods. The method, which we once adopt consistently every year we follow same method. If any change in method from one accounting method to another it results in inconsistency.

(2) Convention of full Disclosure:- This ~~concept~~ convention implies that accounts must be honestly prepared and all the material facts must be disclosed in the financial statements. Disclosure does not mean disclosure of each and every item of information it means disclosure of such information which is of significance to owners, investors and creditors.

(3) Convention of Materiality: According to this convention a detailed record is made for all busines transactions, which are material. Accounts must not be overburdened with unnecessary details. Hence, unimportant matters should be either left out or merged with the other items.

(4) Convention of conservatism:- This is the policy of "playing safe." It takes into consideration all prospective losses but leaves the prospective profits. Where there is a possibility of occurrence of profit or loss, losses to be considered and profits will be overlooked.

20) Classification of Accounts:

The transactions of the business can be classified into three classes of Accounts:—

1) Transactions relating to persons or individuals → personal accounts.
2) Transactions relating to property/assets → Real accounts
3) Transactions relating to Incomes and expenses. Nominal accounts

① PERSONAL ACCOUNT: personal account record the dealings with the trader or companies. So, these are the accounts opened in the name of persons, firms with whom the company deals. personal account can take the following forms.

① Accounts of natural persons like Gopal, Mohan, Shashi A/c.
② Accounts of Artificial persons like Bank A/c, Insurance Company Account, Universal Trading company etc.
③ Accounts of Representative personal Account: for example, if a business is not able to pay salary for the last two months, to all employees. the amount due to the employees will be added and put under one common title "Salaries outstanding Account".

Personal Account

- Natural person's accounts
  - Mohan A/c
  - Shashi A/c
  - Aman A/c
- Artificial Person Account
  - Bank A/c
  - X Company
  - Insurance Company Account
- Representative Personal Account.
  - outstanding Rent
  - Prepaid Insurance

The Rule of personal Account is

Debit what comes in credit what goes out

② REAL ACCOUNT : Accounts relating to properties or assets of a trader are known as Real Accounts.

It Includes ① Tangible assets :- which means such things which can be touched, felt and see. Like plant and machinery, Land & Buildings etc.

② Intangible assets :- The things which are difficult to touch in physical sense. but they can measured in exceptional value.

examples :- Goodwill, patent rights, Trade marks.

Real Account
- Tangible
  - Furniture, stock
  - Cash. etc
- Intangible
  - Goodwill, Trademarks, patents.

The Rule of Real Account is —

Debit what comes in credit what goes out

③ **NOMINAL ACCOUNT** : Nominal account record a traders expenses or gains or losses or incomes. example:- Salaries Account, Rent Account, Commission Account etc.

Nominal Account

- Expenses/losses
  - Ex:- Rent paid
  - Commission Paid
  - Discount allowed
- Incomes/gains.
  - Ex:- Discount Received
  - Commission Received
  - Interest Received.

Rule of Nominal Account

~~Debit all incomes and~~

Debit all expenses and losses
Credit all incomes and gains.

3Q Pass the necessary Journal entries.

2015

Mar 1 Vishal had the following balances cash 75,000 Stock 40,000, furniture 25,000, Prepaid Insurance 18,000, Ajit (debtor) 15,000 Ashish (creditor) 12,000

Mar 2. Cash deposited in to Bank 60,000

Mar 6 Cheque received from Ajit 14,500, Discount allowed 500.

Mar 7 Cheque issued to Ashish 11,800 Discount 200.

Mar 8 Amount withdrawn from Bank for personal use 1000

Mar 9 Cash purchases — 20,000

Mar 10 Cash sales — 50,000

Mar 11 Cash paid for advertising — 100

Mar 12 Purchased goods from B — 2500

Mar 13 Sold goods to Veena — 10,000

Mar 14. Returned goods by B — 120

Mar 15 Sold goods returned by Veena — 1000

Journal of Vishal

Date	Particulars	L/F	Debit	Credit
2015 Mar 1	Cash A/c — Dr		75,000	
	Stock A/c — Dr		40,000	
	Furniture A/c — Dr		25,000	
	Prepaid Insurance — Dr		18,000	
	Ajit — Dr		15,000	
	To Ashish A/c			12,000
	To Capital A/c [Bal. fig]			1,61,000
	[Being commenced Business]			
Mar 2.	Bank A/c — Dr		60,000	
	To Cash A/c			60,000
	[Being cash deposited into Bank]			
Mar 6	Bank A/c — Dr		14,500	
	Discount Allowed A/c — Dr		500	
	To Ajit A/c			15,000
	[Being, cheque received from Ajit and discount allowed]			
Mar 7	Ashish A/c — Dr		12,000	
	To Bank A/c			11,800
	To Discount received			200
	[Being, cheque issued to Ashish. and Discount received.			

8	Drawings A/c — Dr To Bank A/c [Being, withdrawn from Bank for Personal use]	1000	1000
9	purchases A/c — Dr. To Cash A/c [Being, Cash puchases Made]	20,000	20,000
10	Cash A/c — Dr To sales A/c [Being cash sales made]	50,000	50,000
11	Advertising A/c — Dr To Cash A/c [Being advertising paid]	100	100
12.	purchases A/c — Dr To B A/c [Being puchased goods from B on credit]	2500	2500
13.	Veena A/c — Dr To Sales A/c [Being goods sold to Veena. on credit]	10,000	10,000
14	B A/c — Dr To puchase returns A/c [Being, goods puchased from B and returned]	120	120

15	Sales returns A/c — Dr	1000	
	To Veena		1000
	[Being sold goods to veena, returned]		

4Q) What is Double Entry system of Accounting. Explain its advantages and disadvantages.

A. Double Entry system Means Every transaction must has two fold aspect i.e. one party receiving benefit and other party giving the benefit. when we receive something we give something else in return. for example, when we purchase goods for cash, we receive goods and give cash in return.

Similarly when we sell goods on credit, goods are given and the customer becomes debtor. This method of writing every transaction in two accounts is known as Double Entry System. Every transaction is divided into two aspects debit and credit. If one account is debited then the other account is to be credited. The basic principle of Double Entry system of Book keeping is for every debit there is a corresponding credit of equal value.

All the business transactions are recorded in business by following rules of double entry system of accounting. A Trial balance is prepared to verify arithematical accuracy of books of accounts. The Financial statements Profit and loss Account and Balance sheets are prepared.

Profit and Loss account indicates the profit or loss made by the business during that particular accounting period. While the balance sheet presents the true financial position of the business during that particular accounting period.

ADVANTAGES

The advantages of double entry system are as follows—

1) COMPLETE RECORD OF TRANSACTIONS: It records both the aspects of a transaction. Thus, a complete and reliable record of all the business transactions are provided.

2) Arithmetical Accuracy:- As both the aspect of debit and credit transactions are recorded, It is possible to prepare trial balance and check the arithmetical accuracy of books of accounts.

3) Ascertainment of financial result: The profit and loss account is prepared to find out the profit or loss earned or suffered during a given period.

4) Ascertainment of financial position: The balance sheet of the business is prepared to ascertain the financial position on a particular date i.e the amount of Assets liabilities and capital.

5) Helps in comparison: the double entry system enables businessman to ascertain purchases, sales, expenses, Income assets, liabilities of the business for the current year.

So, that to make a comparison with previous year activities, which helps management to take appropriate decisions.

⑥ Detection of frauds: Double entry system is a systematic record of all transactions. So, misappropriation and frauds can be easily detected in business.

Disadvantages

① Complex in nature: Double Entry System is complex in nature as it has to follow lot of rules and regulations of accounting standards and accounting principles.

② Costly:- this system needs to maintain a number of account books. Trained and skilled manpower is also essential for it. Advanced and expensive accounting Software also requires a large amount of money. So, simply its very costly.

③ Not suitable for Small business: In Double entry system a businessman has to keep many books which is not suitable for small concerns. A small business man simply keep the list of Assets, liabilities, bank balance, debtors and creditors on notebook under single entry system.

④ Flaw regarding historical cost: This system ~~only~~ keeps records of assets according to its historical cost price but it does not keep record of transaction according to its market price, which will not give true picture of financial report.

5Q) From the following Trial Balances prepare Trading, profit and Loss A/c for the year ened 31/3/17 and Balancesheet as on that date

Debit balances	Amount	Credit Balances	Amount
Sundry debtors	52,000	Sundry creditors	22,000
Cash in hand	1,592	Sales	2,92,000
Motor Car	22,000	Capital	70,000
Furniture	3,500		
Purchases	1,95,000		
Sales returns	2,600		
Patents	8,420		
Opening stock	7,000		
Motor Car expenses	11,400		
Rent, Rates & Taxes	6,108		
Insurance premium	2,400		
Machinery	24,000		
Wages	23,600		
General expenses	2,680		
Carriage Inwards	2,040		
Carriage Outwards	1,130		
Discount	500		
Fuel	6,430		
Drawings	8,000		
	3,84,000		3,84,000

Dr Trading & P&L A/c for the year ended 31/3/2017 Cr

Particulars	Amount	Particulars		Amount
To Opening stock	7,000	By Sales	2,92,000	
To purchases	1,95,000	Less Sales returns	2600	2,89,400
To Wages	23,600	By closing stock		35,000
To Carriage Inwards	2,040			
To fuel	6,430			
To Gross profit c/d [Transfer to P&L A/c]	~~1,03,190~~ 90,330			
	3,24,400			3,24,400

Particulars	Amount	Particulars	Amount
To Motor Car expenses	11,400	By Gross profit b/d	90,330
To Rent, Rates & Taxes	6,108		
To Insurance premium	2,400		
To General expenses	2,680		
To Carriage outwards	1,130		
To Discount	500		
To Net profit c/d [Transfer to Capital A/c]	66,112		
	90,330		90,330

Balance sheet as on 31/3/17

Liabilities		Amount	Assets	Amount
Capital	70,000		Sundry debtors	52,000
less drawings	8000		Cash in hand	1592
	62,000		Motor Car	22,000
add Net profit	66,112	1,28,112	Furniture	3,500
Sundry creditors		22,000	Patents	8420
			Machinery	24,000
			Closing stock	35,000
			Suspense A/c	3600
		1,50,112		1,50,112

In the above problem, even though the trial balance is given as tallied, But actually its not tallied. the Dr side is showing the grand total of 3,80,400, Therefore we create a suspense a/c on Dr side, [May be any item got Missed] with the difference of amount i.e 3600 [3,84,000 − 3,80,400].

NOTE:- When you are doing problem, it is compulsory to check whether Dr and Cr is tallied or not.

UNIT - IV

① TRIAL BALANCE

A Trial Balance is a statement containing debit and credit balances of various accounts taken out from ledger books as on particular date. A Trial Balance is a summary of all accounts contained in ledger book. Trial Balance must agree as on a give date i.e the total of debit balances must be equal to the total of credit balances. If it does not agree, it means there are arithmetical errors in the books of accounts. Incase, If the firm is unable to locate the errors at the time of preparation of accounts, the difference in trial Balance will be placed in account called Suspense account and it will be carried to Balance sheet. For preparing trial balance first we should understood, which accounts goes under debit & credit balances. The proforma ~~of~~ Balance sheet are:-

Particulars	Debit	Credit
All Assets	xxx	
All Liabilities		xxx
All expenses / Losses	xxx	
All Incomes / Gains	xxx	
Purchases & Sales return	xxx	
Sales & purchase return		xxx

② JOURNAL

Journal is the first book in which transactions are recorded day wise. It is also called as Day book or Book of original entry or first entry.

The process of recording a transaction in Journal called Journalising. Journal analyses various transactions into debit and credits. So, that they could be easily posted into ledger. The proforma of Journal is

Date	Particulars	L/F	Amount (Debit)	Amount (Credit)
2021 Jan 1	Purchases A/c —— Dr To Cash A/c [Being goods purchased on cash]		xxx	xxx

③ LEDGER

Ledger is a book that contains several accounts. The process of preparation of accounts from the Journal into ledger is called posting in the ledger. The format of ledger account is of two parts. ① Left hand side is called Debit side (Dr) and ② Right hand side is called credit side (Cr). Debit side starts with "To" and credit side starts with 'By'.

Dr — Debit side | Credit side — Cr

Date	Particulars	J/F	Amount	Date	Particulars	J/F	Amount

Posting into ledger is made from Journal entries passed in the Journal. Every Journal Entry have to be posted to their respective accounts in ledger. For example, In a Journey entry → Cash A/c ~~is~~ debited and Sales A/c is credited. (i.e) Cash A/c — Dr
To Sales A/c.

As Cash Account is Debited, in cash account on the Debit side we write "To Sales A/c". Similarley in Sales A/c, as Sales is credited, we write on credit side with "By Cash A/c"

Dr CASH A/c Cr

Date	Particulars	J/F	Amount	Date	Particulars	J/F	Amount
xx	To Sales A/c		xxx				

Dr SALES A/c Cr

Date	Particulars	J/F	Amount	Date	Particulars	J/F	Amount
					By Cash A/c		xxx

(4) Balancesheet

Balance sheet is a statement of Assets and liabilities as on a given date. It shows true and fair view of financial position of a business on a given date.
Balance sheet is a statement not an Account. It does not have debit side or credit side. It has assets and liabilities. Balance sheet potrays Accounting equation

where Assets = Equity [Capital + Liabilities]. the Format of Balance sheet is —

Balance sheet as on 31/12/xx

Liabilities	Amount	Assets	Amount
Capital.	xxx	~~Fixed Assets~~	
Long term liabilities	xxx	Land & Buildings	xxx
S. Creditors	xxx	Plant & Machinery	xxx
		Current Assets	
		Cash	xxx
		Bank	xxx
	xxxx		xxxx

⑤ Define Accounting & its significance

According to American Institute of Certified public Accountants [AICPA] defines "Accounting as an art of recording, classifying and summarising in a significant manner and in terms of money and events which are, in part at least of a financial character and interpreting the results thereof".

Accounting is useful for every business organisation to monitor the business activities, to know profit or loss for a given period, shows financial position for a given period, to communicate the information to the interested parties. Accountancy begins where Book keeping ends.

Accounting means the compilation of accounts in such a

⑥ ~~Accounting cycle~~

way that one is in a position to know the state of affaires of business.

(6) ACCOUNTING CYCLE

Accounting cycle covers all the important stages in accounting. They include process of preparing Jounal, Ledger, Trial Balance and Final Accounts. The moment Transactions takes place in business recorded in first book called Jounal. From Jounal, entries are posted into ledger accounts. On the basis of balances shown by ledger accounts, a statement showing debit and credit balances is prepared to ensure arithmetic accuracy of the accounts. This statement is called trial Balance. From Trial Balance information final accounts are prepared. It includes Trading Account Profit and loss Account and Balancesheet. With preparation of final Accounts for that year Accounts are closed. Again cycle begines with a transaction occurs in next year and recorded in Jounal and so on. Again the accounting cycle continues.