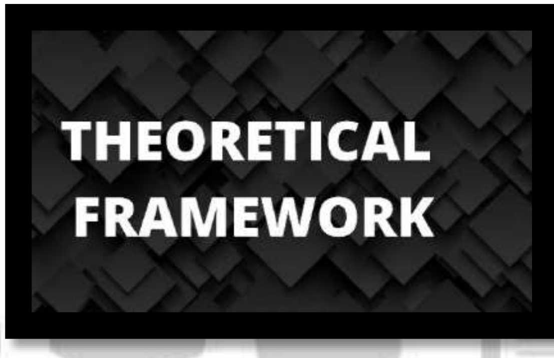
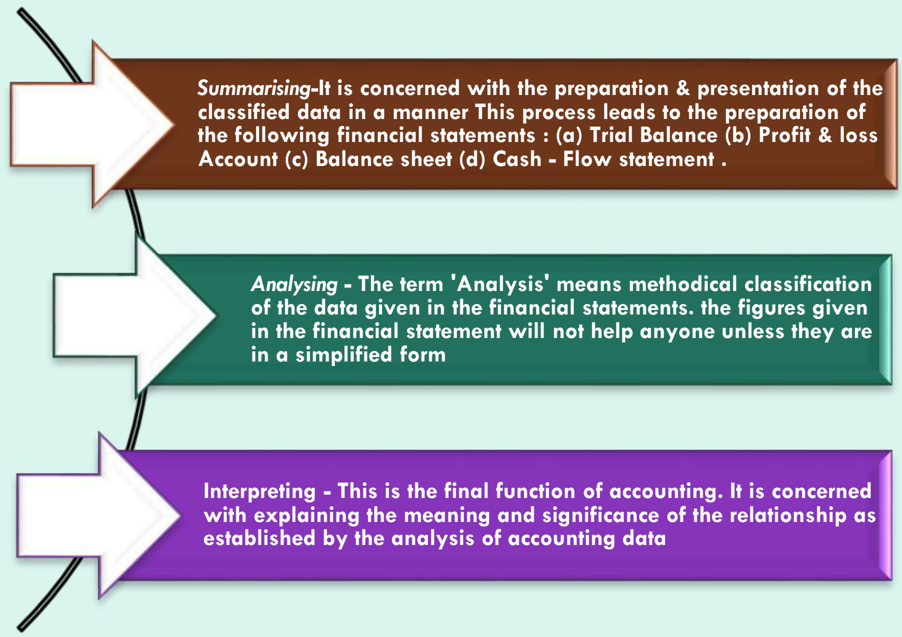
CHAPTER – 1
THEORETICAL FRAMEWORK



UNIT: 1
MEANING & SCOPE OF ACCOUNTING

Definition of accounting	"Accounting is the art of recording, classifying & summarizing in a significant manner & in terms of money, transactions & events which are, in part at least, of a financial character, & interpreting the result thereof"
Procedural aspects of accounting	Procedure of accounting can be basically divided into 2 parts: Generating financial information & using the financial informationGenerating financial information Recording- this is the basic function of accounting. All business transactions of a financial character, as evidenced by some documents such as sales bill, pass book, salary slip etc. are recorded in the books of accounts. Recording in book called 'Journal' Classifying – Classification is concerned with the systematic analysis of the recorded data, with a view to group

transactions or entries of one nature at one place so as to put information in compact and sable form. The book containing classified information is called 'Ledger'. This book contains on different pages, individual account heads under which, all financial transactions of similar nature are collected.



<u>Using the financial information</u>-
The owners or the management of the enterprise, commonly known as internal users, use the accounting information in an analytical manner to take the valuable decisions for the business.
So, the information served to them is presented in a different manner to the information presented to the external users. Even the small details which can affect the internal working of the business are given in the management report while financial statements presented to the external users contain key information.

Objectives of accounting	Systematic recording of transactions Public Ascertainment of the financial position of the business Ascertainment of the result Providing information to the users for rational decision –

	making To know the solvency position
Function of Accounting	• Management • Measurement • Forecasting • Complete Recording of Transaction • Decision Making • Control
SUB – FIELDS OF ACCOUNTING	
Financial Accounting	It covers the preparation & interpretation of financial statement. Its records transactions which had already been occurred. The final step of financial accounting is the preparation of profit & loss accounting and the balance Sheet. It primarily helps in determination of the net result for an accounting period and the financial position as on the given date.
Management Accounting	It is concerned with internal reporting to the managers of a business unit. To discharge the functions of stewardship, planning, control & decision – making, the management needs variety of information.
Cost Accounting	"The process of accounting for cost which begins with the recording of income & expenditure or the bases on which they are calculated & ends with the preparation of periodical statements & reports for ascertaining and controlling Costs."
Social Responsibility	The demand for social responsibility accounting stems from increasing social awareness about the undesirable by-products of economic activities. As already discussed

Accounting	earlier, social responsibility accounting is concerned with accounting for social costs incurred by the enterprise and social benefits created.
Human Resource Accounting	Human resource accounting is an attempt to identify, quantify & report investments made in human resource of an organization that are not presently accounted for under conventional accounting practice

USERS OF ACCOUNTING INFORMATION

INVESTORS	They provide risk capital to the business. They need information to assess whether to buy, hold or sell their investment. Also, they are interested to know the ability of the business to survive, prosper & to pay dividend
EMPLOYEES	Growth of the employees is directly related to the growth of the organization and therefore, they are interested to know the stability, continuity and growth of the enterprise
LENDERS	They are interested to know whether their loan – principal and interest will be paid when due.
Suppliers & Creditors	They are also interested to know the ability of the enterprise to pay their dues, that help them to decide the credit policy for the relevant concern, rates to be charged & so on. Sometimes, they also become interested in long-term continuation of the enterprise
Customers	Customers are also concerned with the stability & profitability of the enterprise because functioning is more or less dependent on the supply of goods

Government & their agencies	They regulate the functioning of business enterprises for public good, allocate scarce resource among competing enterprises, control prices, charge excise duties & taxes, and so they have continued interest in the business enterprise

UNIT – 2

ACCOUNTING CONCEPTS, PRINCIPLES & CONVENTIONS

ACCOUNTING CONCEPT	Accounting concepts define the assumptions on the basis of which financial statements of a business entity are prepared Certain concepts are perceived, assumed and accepted in accounting to provide a unifying structure and internal logic to accounting process
ACCOUNTING PRINCIPLES	"Accounting principles are a body of doctrines commonly associated with the theory and procedures of accounting serving as an explanation of current practices and as a guide for selection of conventions or procedures where alternatives exist"
ACCOUNTING CONVENTIONS	Accounting conventions emerge out of accounting practices only known as accounting principles, adopted by a rations over a period of time These conventions are cert Bryce and practitioner

CONCEPTS ON WHICH ACCOUNTING IS BASED

Entity concept: Entity are that business enterprise is separate identity apart from its owner. Accountants nuts treat a business as distinct from its owner

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Money measurement concept: as per this concept, only those transactions, which can be measured in terms of money are recorded

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Periodicity concept: This is also called the concept of definite accounting period. As per going concern concept an indefinite life of the entity is assumed

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Accrual concept: Under accrual concept, the effects of
transactions and other events are recognised on mercantile basis

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Matching concept: In this concept, all expenses matched withthe revenue of that period should only be taken into
consideration

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Cost concept. By this concept the value of an asset is to be determined on the basis of historical cost.

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Realisation concept It closely follows the cost concept. Any change in value of an asset is to be recorded only when the business realises it.

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Conservatism: Conservatism states that the accountant should not anticipate income and should provide for all possible losses.

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	Consistency: in order to achieve comparability of the financial statements of an enterprise through time, the accounting policies are followed consistently from one period to another, a change in an accounting policy is made only in certain exceptional circumstances ↓ Materiality: Materiality principle permits other concepts to be ignored, If the effect is not considered material. This principle is an exception to full disclosure principle
Fundamental Assumptions Accounting	GOING CONCERN → CONSISTENCY → ACCRUAL
Financial Statements	The financial statements are basic means through which the management of an entity makes public communication of the financial information along with selected quantitative details.

UNIT – 4

CAPITAL AND REVENUE EXPENDITURES & RECEIPTS

CAPITAL EXPENDITURE	Money spent by a business or organization on acquiring or maintaining fixed assets, such as land, buildings, and equipment
REVENUE EXPENDITURE	An amount that is expensed Immediately-thereby being matched with revenues of the current accounting period,
Nature of business	The nature of business is a very important criterion in separating an expenditure between capital and revenue
Recurring nature of expenditure	if the frequency of an expense is quite often in an accounting year then it is said to be an expenditure of revenue nature while non-recurring expenditure is infrequent in nature and do not occur often in an accounting year.
Purpose of expenses	Expenses for repairs of machine may be incurred in course of normal maintenance of the asset. Such expenses are revenue in nature
Effect on revenue generating capacity of business	The expenses which help to generate Income revenue in the current period are revenue in nature and should be matched against the revenue earned in the current period.
Materiality of the amount involved	Relative proportion of the amount involved is another important consideration in distinction between revenue and capital

UNIT – 5

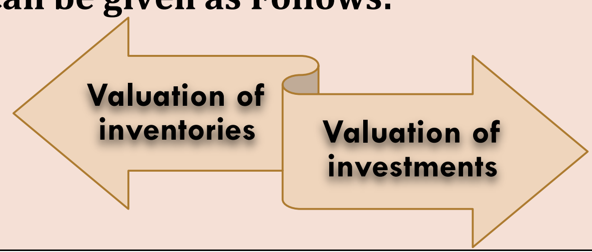
CONTINGENT ASSETS & CONTINGENT LIABILITIES

BASIC TERMS:

CONTINGENT ASSETS	 A possible asset arises from past events and there existence will be confirmed onlyt after occurence or Non - occurence of one or more uncertain future events
CONTINGENT LIABILITIES	 A POSSIBLE OBLIGATION ARISING FROM PAST EVENTS AND MAY ARISEN FUTURE DEPENDING ON THE OCCURRENCE OR NON OCCURRENCE OF ONE OR MORE UNCERTAIN FUTURE EVENTS

Unit – 6

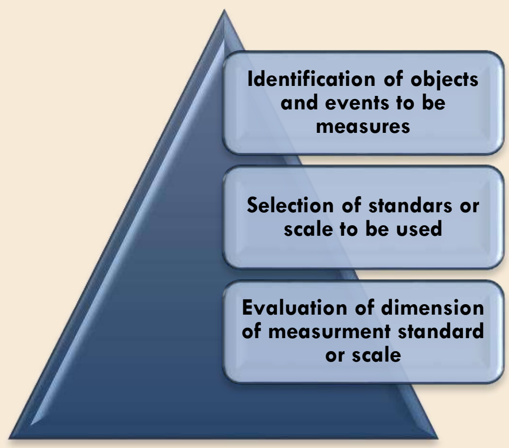
Accounting policies

ACCOUNTING POLICIES	Accounting Policies refer to specific accounting principles and methods of applying the principles adopted by the enterprise in the preparation and presentation financial statements the areas where different accounting policies are frequently encountered can be given as Follows: 

CHANGE IN ACCOUNTING POLICIES	A change in accounting policies should hemade in the following conditions: Its required by some state or for compliance with an Accounting Standard, Change would result in more appropriate presentation of financial statements

Unit – 7

Accounting as a measurement discipline – valuation principles, accounting estimates

MEANING OF MEASUREMENT	Measurement is vital aspect of accounting, primarily transactions and events are measured in terms of money
Elements OF MEASUREMENT	
Valuation Principles	There are 4 generally accepted measurement bases or valuation principles there are: • Historical cost • Current cost • Realizable Value • Present Value

UNIT – 8

ACCOUNTING STANDARDS

FORMULATION OF ACCOUNTING STANDARDS

ACCOUNTING STANDARDS	Accounting as a 'language of business' communicates the financial results of an enterprise to various stakeholders by means of financial statements. If the financial accounting process is not properly regulated, there is possibility of financial statements being misleading, tendentious and providing a distorted picture of the business, rather than the true.
OBJECTIVES OF ACCOUNTING STANDARDS	Accounting Standards standardise diverse accounting policies with a view to: • eliminate the non-comparability of financial statements and thereby improving the reliability of financial statements; and • provide a set of standard accounting policies, valuation norms and disclosure requirements
BENEFITS AND LIMITATIONS OF ACCOUNTING STANDARDS	Standards reduce to a reasonable extent or eliminate altogether confusing variations in the accounting treatments used to prepare financial statements. There are certain areas where important information is not statutorily required to be disclosed. The application of accounting standards would tax limited extent, facilitate comparison of financial statements of companies situated in different parts of the world and also of different companies situated in the same country
ACCOUNTING STANDARDS	Accounting as a language of business communicates the possibility of financial statements being misleading tendentious and providing a distorted picture of the financial results of an enterprise to various stakeholders by means of financial statements. If the financial accounting process is not properly regulated, there isbusiness, rather than the true.

UNIT – 9

INDIAN ACCOUNTING STANDARDS

INTERNATIONAL FINANCIAL REPORTING STANDARD AS GLOBAL STANDARDS	**The term IFRS comprises IFRS issued by IASB; IAS issued by International Accounting Standards Committee (IASC); Interpretations issued by the Standard Interpretations Committee (SIC) and the IFRS Interpretations Committee of the IASB.**
BENEFITS OF CONVERGENCE WITH IFRS	
The Economy:	**When the markets expand globally the need for convergence increases since the convergence benefits the economy by increasing growth of its international business,**
Investors	**A strong case for convergence can be made from the viewpoint of the investors who wish to invest outside their own country. Investors want the information that is more relevant, reliable, timely and comparable across the jurisdictions.**

Question 1

State with reasons whether the following statement is true or false:

- **Accounting principle is general rule followed in preparation of FinancialStatements.**

- **Capital is equal to assets less external liabilities.**

Answer:

- **True:** Accounting principles suggests the rules of action which are universally accepted by the accountants for the recording of accounting transactions
- **True:** Capital + Reserves &Surplus (internal liabilities)–Capital + Liabilities = Assets

Question 2

Transactions and events are guides by generally accepted accounting principles and the transactions and events are guided by those principles.

Answer:

TRUE Every country adopts some generally accepted accounting principles and thetransactions and events are guided by those principles.

Question 3

State with reasons whether the following statement is true or false

- **Goods worth 600 taken by the proprietor for personal use should be credited to purchase account.**
- **Rent paid account is a Nominal Account whereas, Rent received account is a Real account**
- **Amount paid to Management company for consultancy to reduce the working expenses is revenue expenditure.**

Answer:

True: Goods taken by the proprietor for personal use should be debited to Drawings

Account and Credited to Purchase Account

False: -Rent is an either income or expense so it is a nominal account whether it is received or receivable or paid or payables.

False: -Amount paid or payable to Management Company for consultation e reduce the working expenses is deferred revenue expenditure Such expenditure gives tong term benefit to the business entity and it cannot be realised in the market directly

Question 4

What do you mean by Book Keeping?

Answer:

Bookkeeping is an activity concerned with the recording of financial data relating to business operations in a significant and orderly manner It covers procedural aspects of accounting work and traces record keeping function. Obrony book ping procedures are governed by the end product, he financial statements

The term "financial statements means Profit and Loss Account and Balance Sheet including

Schedules and Notes forming part of Accounts.

Question 5

Gives objective of Accounting

Answer:

Objectives of Accounting are: -

- **Systematic recording of transactions -** Basic objective of accounting is to systematically record the financial aspects of business transactions i.e. book-keeping. These recorded transactions are later on classified and summarized logically for the preparation of financial statements and for their analysis and interpretation.

- **Ascertainment of results of above recorded transactions -** Accountant prepares profitand loss account to know the results of business operations for a particular period of time. If revenue exceed expenses then it is said that business is running profitably but if expenses exceed revenue then it can be said that business is running under loss. The profit and loss account helps the management and different stakeholders in taking rational decisions. For example, if business is not proved to be remunerative or profitable, the cause of such a state of affair can be investigated by the management for taking remedial steps.

- **Ascertainment of the financial position of the business -** Businessman is not only interested in knowing the results of the business in terms of profits or loss for a particular period but is also anxious to know that what he owes (liability) to the outsiders and what he owns (assets) on a certain date. To know this, accountant prepares a financial position statement popularly known as Balance Sheet. The balance sheet is a **statement of assets and**

liabilities of the business at a particular point of time and helps in ascertaining the financial health of the business,

- **Providing information to the users for rational decision-making -** Accounting as a 'language of business' communicates the financial results of an enterprise to various stakeholders by means of financial statements. Accounting aims to meet the information needs of the decision-makers and helps them in rational decision-making.

- **To know the solvency position -** By preparing the balance sheet, management not only

reveals what is owned and owed by the enterprise, but also it gives the information regarding concerns ability to meet its liabilities in the short run (liquidity position) and also in the long-run (solvency position) as and when they fall due.

Question 6

Differentiate Book Keeping & Accounting.

Answer:

S no.	Book - Keeping	Accounting
1.	It is a process concerned with recording of transactions	It is a process concerned with summarizing of the recorded transactions
2.	It constitutes as base for accounting	It is considered as a language of the business
3.	Financial statements do not form part of this process	Financial statements are prepared in this process on the basis of book-keeping records
4.	Managerial decisions cannot be taken with the help of these records	Management takes decisions on the basis of these records.
5.	Financial position of the business cannot be ascertained	Financial position of business is ascertained

	through book-keeping records.	on the basis of the accounting reports.
6.	There is no sub – field of book - keeping	It has several sub fields like financial accounting, management accounting etc.

Question 7
Explain Different function of accounting.
Answer:
The main functions of accounting are as follows:

- **Measurement**: Accounting measures past performance of the business entity and depictsits current financial position.

- **Forecasting**: Accounting helps in forecasting future performance and financial position of the enterprise using past data.

- **Decision-making**: Accounting provides relevant information to the users of accounts to aid rational decision-making

- **Comparison & Evaluation**: Accounting assesses performance achieved in relation to
 targets and discloses information regarding accounting policies and contingent liabilities which play an important role in predicting, comparing and evaluating the financial results, Control: Accounting also identifies weaknesses of the operational system and providesfeedbacks regarding effectiveness of measures adopted to check such weaknesses.

- **Regulation and Taxation**:GovernmentAccounting provides necessary information to thegovernment to exercise control on the entity as well as in collection of tax revenues.

Question 8
What are the Accounting Conventions?
Answer:

Accounting conventions Accounting conventions emerge out of accounting practices, commonly known as accounting principles, adopted by various organizations over a period of time. For details, refer para 24

Question 9

What are the Basic Fundamental Accounting Assumptions of Accounting?

Answer:

Fundamental accounting assumptions: There are three fundamental accounting assumptions: Going Concern. Consistency and Accrual. If nothing has been written about the fundamental accounting **assumption in the** financial statements then it is assumed that they have already been followed in their preparation of financial statements,

Question 10

Distinguish between: Money measurement concept and matching concept Going concern and cost concept.

Answer:

Distinction between Money measurement concept and matching concept:

As per Money Measurement concept, only those transactions, which can be measured in terms of money are recorded. Since money is the medium of exchange and the standard of economic value, this concept requires that those transactions alone that are capable of being measured in terms of money be only to be recorded in the books of accounts. Transactions and events that cannot be expressed in terms of money are not recorded in the business books.

In Matching concept, all expenses matched with the revenue of that period should only
be taken into consideration. In the financial statements of the organization if any revenue is recognized then expenses related to earn that revenue should also be recognized.
(ii) Distinction between Going concern and cost concept, Going Concern Concept

The financial statements are normally prepared on the assumption that an enterprise is a going concern and will continue in operation for the foreseeable future.

Cost Concept: - By this concept, the value of an asset is to be determined on the basis of historical cost, in other words, acquisition cost. For details refer para 2.5.

Question 11

Write a short note onAccrual basis of accounting.

Answer:

Accrual basis of Accounting: Accrual or mercantile basis accounting refers to a system of recording revenues and expenses whether or not they have been received or paid in cash at the time recording Accounting on accrual basis signifies that owner's equity is affected by the profit earned or loss suffered by an enterprise during accounting period and not as money is received or paid. Therefore, while ascertaining the profit or loss not only the expenses which have been paid in cash should be considered, also expenses which have become due though not paid should take into account

Similarly, all the incomes earned during the accounting peri should be considered

whether they have been received in cash or not

Question 12

Write a short note onGoing Concern.

Answer:

Going concern concept: It means that the business will go o indefinitely Le the business is not going to be liquidated in foreseeable future. This concept is a fundamental to the accounting theory. The Balance sheet is prepared on the basis of this concept and the prepay expenses are shown as assets in the B/S because of this concept only. The creditors supply the goods and services expecting to continuation of business for a long period

Question 13

What is Dual aspect principal.

Answer:

Dual Aspect Principle: It is the core of accounting according to this principle all business transactions involve two-fold aspects and both the aspects have to be recorded in the books of account.

In order to understand this principle, it is necessary for us to understand simultaneously the meaning of three terms (i) Assets (ii) Capital (iii) Creditors External liabilities). Since. total assets of the business are acquired out of the money contributed by the proprietors and creators of the business, it is easy to express the effects of the transaction as under.

Capital + Liabilities = Assets

The above relationship is known as the "Accounting Equation."

Note: Since all this is looked at from the business point of view, there is a dual aspect of all transactions

The system of recording transaction based on this concept is called "double entry system".

Question 14

Explain the difference between the following:

1) Commission and Discount.

Answer:

Commission: Commission may be defined as the remuneration relating to services performed in connection with the purchases, sales, or other types of business transactions. Generally, commission is provided on profits. It is allowed as a percentage of net profit before charging any such commission. tis shown on the debit side of P&L A/c as an expense.

Discount: Discount is an allowance or a deduction allowed from an amount Due. There are three types of discounts permissible:

- **Cash Discount**: Which is allowed to a debtor on prompt payment of cash.
- **Trade Discount**: Which is allowed to a buyer on the printed price lists.
- **Quantity Discount**: Which is allowed to a buyer on the catalogue price on a purchase of items or goods. Discount allowed is shown on the debit side of the P&L A/c and discount received is shown on the credit side of the P & L A/c

Question 15

Differentiate Capital and Revenue Expenditure

Answer:

BASIC	CAPITAL EXPENDITURE	REVENUE EXPENDITURE

OBJECT	It results in acquisition of fixed asset which meant for use and not are resale.	It does not result in acquisition of any fixed asset
Benefit of such expense	It results in improving the earning capacity of fixed asset	It results in the repairs & maintenance of the business assets.
Period of use	The benefit of such expenditure will be for more than one year	The benefit of such expenditure expires during the year
Written off	All items of capital expenditure, which are not written off, are shown in the B/S assets	All revenue items the benefit of which has exhausted during the year are transferred to trading P&L
Carry forwarded	These items are carried forwarded to the next year.	These items are not carried forward to the next year but whose benefit has not expired are carried forward to the next year

Question 16

Explain Conservatism Principle.

Answer:

Conservatism Principle: Conservatism means taking the gloomy side of the situation. Future is uncertain. Through an estimate is made about future events and circumstances, but no one can guess the future with perfect certainty in business. Hence, some arrangements or provision is made to meet the future uncertainties. A very sincere business makes an estimate of future loss and then some provision for it is made such as provision for bad debts. Businessmen mostly ignore the items of future profit. This tendency is termed as conservatism and it is very natural tendency and is in existence since loon

Question 17

What is the concept of consistency Principal?

Answer:

Consistency Principle: Accounting rules, practices and conventions should be continuously observed and applied i.e. these should not change from 1 year to another. Continuation of one practice for a number of years indicate consistency e.g. if an asset is depreciation on diminishing balance method in 1 year the same method of depreciation be adopted in other year also.

Question 18

What is Preliminary and prepaid Expenses.

Answer:

Preliminary Expenses

Expenses relating to the formation of an enterprise. These include legal, accounting and
share issue expenses incurred for formation of the enterprise.

Prepaid Expense

Payment for expense in an accounting period, the benefit for which will accrue in the subsequent accounting period(s).

Question 19

What do mean by Floating charges.

Answer:

A general charge on some or all assets of an enterprise which are not attached to specific assets and are given as security against a debt.

Question 20

Define the following.

1. Prime cost

2. Revaluation Reserve.

Answer:

1. The total cost of direct materials, direct wages and other direct production expenses.
2. A reserve created on the revaluation of assets or net assets of an enterprise represented by the surplus of the estimated replacement cost or estimated market values over the book values thereof.

Question 21

List out Difference between provision and Contingent Liability.

Answer:

S No.	Provision	Contingent liability
1.	Provision is a present liability amount, which can be measured reliably by using a substantial degreeof estimation.	A contingent liability is a possible obligation that may or may not crystallise depending on the occurrence or non – occurrence of one or more uncertain future events.
2.	A provision meets the recognition criteria	A contingent liability fails to meet the same.
3.	Provision is recognised when (a) an enterprise has a present obligation arising from past events; an outflow of resources embodying economic benefits is probable and (b) a reliable estimate can be made of the amount of the obligation	A contingent liability includes present obligations that do not meet the recognition. Criteria because either it is not probable that settlement of those obligations will require outflow of economic benefits, or the amount cannot be reliably estimated
4.	If the management estimates that it is probable that the settlement of an obligation will result in outflow of economic benefits, it recognises a provision in the balance sheet.	If the management estimates, that it is less likely that any economic benefit will outflow the firm to settle the obligation, it discloses the obligation as a contingent liability

Question 22

What are the conditions in which accounting Policies can be changed?

Answer.:A change in accounting policies should be made in the following conditions:

It is required by some statute or for compliance with an Accounting Standard.

Change would result in more appropriate presentation of financial statement.

Change in accounting policy may have a material effect on the items of financial statements. For example, if depreciation method is changed from straight-line method to written-down value method, or if cost formula used for inventory valuation is changed from weighted average to FIFO, or if interest is capitalized which was earlier not in practice, or if proportionate amount of interest is changed to inventory which was earlier not the practice, all these may increase or decrease the net profit. Unless the effect of such change in accounting policy is quantified, the financial statements may not help the users of accounts. Therefore, it is necessary to quantify the effect of change on financial statement items like assets, liabilities, profit/loss.

Question 23

What are the Objective of Accounting Standards?

Answer:

The whole idea of accounting standards is centredaround harmonisation of accounting policies and practices followed by different business entities so that the diverse accounting practices adopted for various aspects of accounting can be standardised. Accounting Standards standardise diverse accounting policies with a view to:

eliminate the non-comparability of financial statements and thereby improving the reliability of financial statements, and provide a set of standard accounting policies, valuation norms and disclosurerequirements.

Accounting standards reduce the accounting alternatives in the preparation of financial statements within the bounds of rationality, thereby ensuring comparability of financial statements of different enterprises.

Question 24

State the advantages of setting Accounting Standards.

Answer:

The main advantage of setting accounting standards is that the adoption and application of accounting standards ensure uniformity, comparability and qualitative improvement in the preparation and presentation of financial statements.

The other advantages are: Reduction in variations; Disclosures beyond that required by law and Facilitates comparison

Question 25

What is the Separate entity principle?

Answer:

Separate entity principle: It means that the business is tr as a separate and distinct from the proprietor. Al transactions of the business are recorded in the books of business from the point of view of the business as an entity proprietor is treated as a creditor to the extent of his capital.

Question 26

Who are the users of accounts?

Answer:

Users of accounts can be listed as Investors, Employees, Lenders, Suppliers and Creditors, Customers, Govt. and their agencies, public and Management.

Question 27

What is the Procedural Aspect of Accounting?

Answer:

On the basis of the definitions, procedure of accounting can be basically divided into two parts:

- Generating financial information and
- Using the financial information.

Question 28

Explain the conditions must be Satisfied by the Accounting Principles.

Answer:

"Accounting principles are a body of doctrines commonly associated with the theory and procedures of accounting serving as an explanation of current practices and
as a guide for selection of conventions or procedures where alternatives exist."
Accounting principles must satisfy the following conditions: -

- ✓ They should be based on real assumptions:
- ✓ They must be simple, understandable and explanatory
- ✓ They must be followed consistently,
- ✓ They should be able to reflect future predictions
- ✓ They should be informational for the users.

Question 29

Explain Term Intangible Assets with Examples.

Answer:

Asset which does not have a physical identity an intangible asset is an asset that is not physical in nature. Goodwill, brand recognition and intellectual property, such as patents, trademarks and copyrights, are all intangible assets. Intangible assets exist in opposition to tangible assets, which include land, vehicles, equipment and inventory

Question 30

Define.

1. **Unexpired Cost**
2. **Unissued Share Capital**

Answer:

Unexpired Cost

That portion of an expenditure whose benefit has not yet been exhausted.

Unissued Share Capital

That portion of the authorised share capital for which shares have not been offered for subscription

Question 31

What do mean by Shareholder equity.

Answer:

Shareholders' Equity The interest of the shareholders in the net assets of a corporate enterprise. However, in the case of liquidation it is represented by the residual assets after meeting prior claims.

Question 32

State the reason whether the following statements are "True' or False'.

1.Expense incurred on the repairs and white washing for the first time on purchase of an old building is Revenue Expenses.

2.Expenses in connection with obtaining a license for running the cinema is

Capital Expenditure.

Answer:

1. **False**: Repairing and white washing expenses for the first time of an old building are incurred to put the building in usable condition. These are the part of the cost ofbuilding. Accordingly, these are capital expenditure,

2. **True**: The Cinema Hall could not be started without license. Expenditure incurred to obtain the license is pre-operative expense which is capitalized. Such expenses are amortized over a period of time.

Question 33

Name those generally accepted measurement bases or valuation principles.

Answer:

There are four generally accepted measurement bases or valuation principles. These are:

- ✓ Historical Cost;
- ✓ Current Cost:
- ✓ Realizable Value;
- ✓ Present Value.

Accounting Concepts

- **Business entity concept:** A business and its owner should be treated separately as faras their financial transactions are concerned.
- **Money measurement concept:** Only business transactions that can be expressed in terms of money are recorded in accounting, though records of other types of transactions may be kept separately.
- **Dual aspect concept:** For every credit, a corresponding debit is made. The recording of a transaction is complete only with this dual aspect.
- **Going concern concept:** In accounting, a business is expected to continue for a fairlylong time and carry out its commitments and obligations. This assumes that the business will not be forced to stop functioning and liquidate its assets at "fire-sale" prices.
- **Cost concept:** The fixed assets of a business are recorded on the basis of their original cost in the first year of accounting. Subsequently, these assets are recorded minus depreciation. No rise or fall in market price is taken into account. The concept applies only to fixed assets.
- **Accounting year concept**: Each business chooses a specific time period to complete a cycle of the accounting process-for example, monthly, quarterly, or annually—as per afiscal or a calendar year.
- **Matching concept:** This principle dictates that for every entry of revenue recorded in a given accounting period, an equal expense entry has to be recorded for correctly calculating profit or loss in a given period.

- **Realisation concept**: According to this concept, profit is recognised only when it is earned. An advance or fee paid is not considered a profit until the goods or services have been delivered to the buyer.

Question 34

Give a definition of Accounting Principle.

Answer:

"Accounting principles are a body of doctrines commonly associated with the theory and procedures of accounting serving as an explanation of current practices and as a guide for selection of conventions or procedures where alternatives exist.

Question 35

Explain the areas in which different accounting policies may be Followed?

Answer:

The following are examples of the areas in which different accounting policies may be adopted by different enterprises.

- Methods of depreciation, depletion and amortisation
- Treatment of expenditure during construction
- Conversion or translation of foreign currency intern's
- Valuation of inventories
- Treatment of goodwill
- Valuation of investments
- Treatment of retirement benefits
- Recognition of profit on long-term contracts
- Valuation of fixed assets
- Treatment of contingent liabilities

Question 36

Define Measurement in brief. Explain the significant elements of measurement.

Answer:

Measurement is vital aspect of accounting. Primarily transactions and eventsare measured in terms of money. Three elements of measurement are:

1. Identification of objects and events to be measured;
2. Selection of standard or scale to be used

3. Evaluation of dimension of measurement standard or scale.

Question 37

Explain the concepts of Capital Expenditure & give some examples or Cost Includes in it

Answer:

As capital expenditure results in increase in the fixed asset of the entity Capital expenditure, as opposed to revenue expenditure, is generally of a one-off kind and its benefit is derived over several accounting periods. Capital Expenditure may include thefollowing:

- Purchase costs (less any discount received)
- Delivery costs
- Legal charges
- Installation costs
- Up gradation costs Replacement costs
- Replacement cost

Question 38

Explain GAAP

Answer:

0Generally accepted accounting principles (GAAP) definition: A set of rules and guidelines developed by the accounting industry for companies to follow when reporting financial data. Following these rules is especially critical for all publicly traded companies.

Question 39

What are the steps for Generating Financial Information Accounting?

Answer:

Generating Financial Information is to be done in Following Ways

- Recording
- Classifying
- Summarizing
- Analysing
- Interpreting
- Communicating

Question 40

Define.
1. Accumulated Depletion
2. Accumulated Depreciation
Answer:
Accumulated Depletion
The total to date of the periodic depletion charges on wasting assets.
Accumulated Depreciation
The total to date of the periodic depreciation charges on depreciable assets.

Question 41

States the Element of Measurement.
Answer:
According to this definition, the three elements of measurement are:

- Identification of objects and events to be measured;
- Selection of standard or scale to be used;
- Evaluation of dimension of measurement standard or scale.

Question 42

Explain the Relationship of Accounting & Law.
Answer:
Accounting and Law: An economic entity operates within a legal environment All transactions with suppliers and customers are governed by the Contract Act, the Sale of Goods Act, the Negotiable Instruments Act, etc. The entity itself is created and controlled by laws. For example, a company is created by the Companies Act and also controlled by Companies Act. Similarly, every country has a set of economic, fiscal and labour laws. Transactions and events are always guided by laws of the land. Very often the accounting system to be followed has been prescribed by the law. For example, the Companies Act has prescribed the format of financial statements for companies.
Banking, insurance and electric supply undertakings may also have to produce financial statements as prescribed by the respective legislations controlling such entities. However, legal prescription about the accounting system is the product of developments in accounting knowledge. That is to say, legislation about accounting system cannot be enacted unless there is a corresponding development in the accounting discipline. In that way accounting influences law and is also influenced by law.

Question 43

What do mean by Depreciable Assets.

Answer:

Depreciable assets are assets whichare expected to be used during more than one accounting period;And have a limited useful life, and are held by an enterprise for use in the production or supply of goods and services, forrental to others, or for administrative purposes and not for the purpose of sale in the ordinary course of business.

Question 44

What is the Area of Services for Accounting?

Answer:

Some of the services rendered by accountants to the society are briefly mentioned hereunder:

Maintenance of Books of Accounts: An accountant is able to maintain a systematicrecord of financial transactions in order to establish the net result of the transactionsentered into during a period and to state the financial position of the concern as at a particular date.

Statutory Audit: Every limited company is required to appoint a chartered accountant or a firm of chartered accountants as their auditor who are statutorily required to report each year whether in their opinion the balance sheet shows a true and fair view of the state of affairs on the balance sheet date, and the profit and loss account shows a true examines the accounting transactions and also the system, according to which these haveand fair view of the profit or loss for the year.

Internal Audit: It is a management tool whereby an internal auditor thoroughlybeen recorded with a view to ensure the management that the accounts are beingproperly maintained and the system contains adequate safeguards to check any leakageof revenue or misappropriation of property or assets and the operations have beencarried out in conformity with the plans of management.

Taxation: An accountant can handle taxation matters of a business or a person and he can represent that business or person before the tax authorities and settle the tax liability under the statute prevailing. He can also assist in avoiding or reducing tax burden by proper planning of tax affairs,

Management Accounting and Consultancy Services: Management accountant performs an advisory function. He is largely responsible for internal reporting to the management for planning and controlling current operations, decision-making on special matters andfor formulating long-range plans. His job is to collect, analyse, interpret and present all accounting information which is useful to the management.

Financial Advice: Many people need help and guidance in planning their personal financial affairs. An accountant who knows about finances, taxation and family problems is well placed to give such advice. Some of the areas in which an accountant can render financial advice are:

Question 45
What is The Role of Chartered Accountant in Industry?
Answer:
An accountant, though he is a part of the highest planning team is not a planner in an industry. He works with the functional departments and translates the organisation's aims in terms of financial expectations. Therefore, he has to make a thorough study of the business and of individuals in the functional departments, whether they are engineers or salesmen. A qualified accountant will be able to play an important role in performing important functions of a business relating to accounting, costing and budgetary control, estimating and treasury.

Question 46
What are the basic Functions of Accountant?
Answer:
Functions of an Accountant
Accountants in the modern era perform a variety of functions. Their jobs are no longer limited to preparation of financial accounts. Accountants also provide their clients, the government and society in general with many other important services.

- **Maintaining Books of Accounts**

This is the primary function of an accountant, i.e. to perform the functions of accounting. He will maintain a systematic record of all financial transactions of a firm.

- **Statutory Audit**

The laws of our country require a few organizations to be compulsorily audited by an auditor. So limited companies, co-operative societies, companies or firms that have crossed a certain turnover limit etc. So a chartered accountant will minutely study and audit the financial records of the said firm. He will verify that to the best of his judgment the profit and loss statement gives a true and fair representation of the profit/loss earned. And that the Balance Sheet is a trueand fair statement of the company's financial position on the given date.

- **Internal Audit**

Some organizations also opt for internal auditing, which is also done by accountants. Internal auditors work with the management of the firm to review the accounts and the internal system of the firm at regular intervals of time.

- **Taxation**

An accountant is also capable of handling taxation matters for a firm or an individual. He can file tax returns on behalf of his clients. A chartered accountant can also represent his clients in cases in Tribunals and Courts to settle tax liabilities on behalf of them.

- **Cost Accounting**

Accountants also carry out cost accounting, i.e. examine the costing structure of a firm. They record, report, summarize and analyse cost data of organizations. They then developmethods of controlling such costs.

- **Management Accountant**

Management accountant does more than number crunching, he plays an overall advisory role in the management of an organization. They analyse the finances of a company andhelp the management with their functions of planning, decision-making, controlling etc.

- **Financial Advice**

Accountants have widespread knowledge and experience in mar fields and industries. So they are very well equipped to provide their clients with financial advice about a variety of financial matters.

Question 47

One limitation of financial accounting is it provides no control on cost.

True or false?

Answer:

The following statement is True. Financial accounting does not attribute or control costs. There is no proper control of material, labour, overhead costs etc. However, cost accounting makes provision for this.

Question 48

Human Resource Accounting deals with the accounting of physical human asset?

Answer:

This statement is False. Human Resource Accounting deals with the accounting of human assets. which are considered to be the most important assets of the company. Sotheir valuation and contribution to the company must also be recorded.

Question 49

What is the significance of issue of Indian Accounting Standards?Explain in brief.

Answer:

Global Standards facilitate cross border flow of money, global listing in different bourses and comparability of financial statements. The convergence of financial reporting and accounting standards is a valuable process that contributes to the free flow of global investment and achieves substantial benefits for all capital market stakeholders. It improves the ability of investors to compare investments on a global basis and thus lowers their risk of errors of judgment. It facilitates accounting and reporting for companies with global operations and eliminates some costly requirements say reinstatement of financial statements.

Question 50

What Is IFRS?

Answer:

International Financial Reporting Standards (IFRS) are a set of accounting standards developed by the International Accounting Standards Board (ASB) that is becoming the global standard for the preparation of public company financial statements.

Question 51

Explain the periodicity Concept of Accounting,

Answer:

Periodicity concept: This is also called the concept of definite accounting period. As per 'going concern' concept an indefinite life of the entity is assumed. For a business entity it causes inconvenience to measure performance achieved by the entity in the ordinary course of business. If a textile mill lasts for 100 years, it is not desirable to measure its performance as well as financial position only at the end of its life.

So a small but workable fraction of time is chosen out of infinite life cycle of the business entity for measuring performance and looking at the financial position. Generally,one-year period is taken up for performance measurement and appraisal of financial position. However, it may also be 6 months or 9 months or 15 months. According to this concept accounts should be prepared after every period & not at the end of the life of the entity. Usually, this period is one calendar year. We generally follow

Question 52

Define the term inventories & factors involved in it.

Answer:

Inventories are assets:

Held for sale in the ordinary course of business; in the process of production for such sale; origin the form of materials or supplies to be consumed in the production process or in the

Rendering of services.

It is shown as current Assets in the Balance Sheet.

Question 53

State the Reasons whether the statements are true or False

1. **Overhaul expenses of second-hand machinery purchased are Revenue Expenditure.**
2. **Money spent to reduce working expenses is Revenue Expenditure.**

Answer:

1. **False**: Overhaul expenses are incurred to put second-hand machinery in working condition to derive endurable long-term advantage. So it should be capitalised.
2. **False**: It may be reasonably presumed that money spent for reducing revenue expenditure would have technical know-how and tangible fixed

assets if it is in the form of additional replacement of any of the generated long-term benefits to the entity. It becomes part of intangible fixed assets if it is in the form of existing tangible fixed assets. So this is capital expenditure.

Question 54

What does mercantile basis of Accounting Mean?

Answer:

Accrual/Mercantile Basis of Accounting

The method of recording transactions by which revenues, costs, assets and liabilities are reflected in the accounts in the period in which they accrue. The 'accrual basis of accounting includes considerations relating to deferrals, allocations, depreciation and amortization. This basis is also referred to as mercantile basis of accounting

Question 55

Good Pictures Ltd., construct a cinema house and incur the following expenditure duringthe first year ending 30th June, 2011

I. **Second-hand furniture worth Rs. 7,000 was purchased; repainting of the furniture costs Rs. 1,000. Thefurniture was installed by own workmen, wages for this being 2200.**
II. **Expenses in connection with obtaining a license for running the cinema worth 20,000. During the course of the year the cinema company was fined Rs. 1,000, for contravening rules. Renewal fee Rs. 2000for next year also paid.**
III. **Fire insurance, 21,000 was paid on 1st January, 2011 for one year**
IV. **Temporary huts were constructed costingRs. 1200. They were necessary for the construction of thecinema. They were demolished when the cinema was ready. Point out how you would classify the above items.**

Answer:

1.The total cost of the furniture should be treated as 10,200 i.e., all the amounts mentionedshould be capitalised since without such expenditure the furniture would not be available for use. If 1,000 and 2200 have been respectively debited to the Required Account and the Wages Account these accounts will be credited to the Furniture Account.

2. License for running the cinema house is necessary, hence its cost should be capitalised. But the fine of 1,000 is revenue expenditure. The renewal fee for the next year is also revenue expenditure but pertains to the next year; hence, it is a prepaid expense.

3. Half of the insurance premium pertains to the year beginning on 1st July, 2011. Hence such amount should be treated as prepaid expense. The remaining amount is revenue expense for the current year.

4. Since the temporary huts wore necessary for the construction, their cost should be added to the cost of the cinema hall and thus capitalised.

Question 56

Why it is necessary for accountants to assume that business entity will remain a going concern?

Answer:

Going Concern Concept assumes that the business entity will continue its operation for an indefinite period of time. It is necessary to assume so, as it helps to bifurcate revenueexpenditure (i.e. expenditure related to current year), and capital expenditure (i.e. expenditure whose benefits accrue over a period of time). For example, a machinery that costs Rs 1,00,000, having an expected life of 10 years, will be treated as a capital expenditure, as its benefit can be availed for more than one year, whereas, the per year depreciation of the machinery, say Rs 10,000, will be regarded as a revenue expenditure.

Question 57

Discuss briefly the relationship of accounting with.

I. **Economics**
II. **Statistics**
III. **Answer:**

(I) **Accounting and Economics**: Economics is viewed as a science of rational decision-making about the use of scarce resources. It is concerned with the analysis of efficient use of scarce resources for satisfying human wants. This may be viewed either from the perspective of a single firm or of the country as a whole.

Accounting is viewed as a system, which provides data to the users to permit informed judgement and decisions. Some non-accounting data are also relevant for decision making. Still, accounting provides a major database. Accounting overlaps economics in many respects. It contributed a lot in improving the management decision-making process. Buteconomic theories influenced the development of the decision-making tools used in accounting.

(ii) **Accounting and Statistics**: The use of statistics in accounting can be appreciated better in the context of the nature of accounting records. Accounting information is very precise
it is exact to the last paisa. But, for decision-making purposes such precision is not necessary and hence, the statistical approximations are sought. In accounts, all values are important individually because they relate to business transactions. As against this, statistics is concerned with the typical value, behaviour or trend over a period of time or the degree of variation over a series of observations. Therefore, wherever a need arises for only broad generalisations or the average of relationships, statistical methods have to be applied in accounting data.

Question 58

What is the basic accounting equation?

Answer:

The basic accounting equation is, Assets = Liabilities + Capital It means that all the monetary value of all assets of a firm are equal to the total claims, viz. owners and outsiders.

Question 59

I. **If a firm believes that some of its debtors may 'default', it should act on this by making sure that all possible losses are recorded in the books. This is an exampleof the___________concept.**
II. **The fact that a business is separate and distinguishable from its owner isbest exemplified by the ___________Concept.**
III. **Everything a firm owns; it also owns out to somebody. This co-incidence isexplained by ______________ concept.**
IV. **The __________ concept states that if straight line method of depreciation is used in one year, then it should also be used in the next year.**

V. **A firm may hold stock which is heavily in demand. Consequently, the market value thisof this stock may be increased. Normal accounting procedure is to ignore because of the________**

VI. **If a firm receives an order for goods, it would not be included in the sales figure owing to the ________**

Answer:

I. If a firm believes that some of its debtors may 'default', it should act on this by making sure that all possible losses are recorded in the books. This is an example of the **conservatism** concept.

II. The fact that a business is separate and distinguishable from its owner is best exemplified by **the business entity** concept.

III. Everything a firm owns; it also owns out somebody. This co-incidence is explained by the **dual aspect** concept.

IV. The **consistency** concept states that if straight line method of depreciation is used inone year, then it should also be used in the next year.

V. A firm may hold stock which is heavily in demand. Consequently, the market value of this stock may be increased. Normal accounting procedure is to ignore this because ofthe **conservatism**.

VI. If a firm receives an order for goods, it would not be included in the sales figure owing to the **revenue recognition**.

Question 60.

Are the following expenses capital in nature?

I. **Wages paid for installation of fixed assets.**

II. **Expenses of trial run of a newly installed machine.**

III. **Money deposited with the wholesaler as security**

IV. **Money paid to Mahanagar Telephone Nigam Ltd. (MTNL) 78,000 for installing Telephone in the office.**

V. **Diwali advance to employees.**

VI. **Money advanced to suppliers for booking of goods.**

Answer:

I. Expenses incurred including wages for installation of any fixed asset is capital expenditure in nature.

II. Expenses incurred for trial run of a newly installed machinery is capital expenditure in nature.

III. Money deposited as security is not an expenditure item

IV. Money deposited with MTNL for installation of telephone is not expenditure item. This is trended as an asset
V. Diwali advance to employees is not an expense item.
VI. Money advanced to supplies for booking goods is not an expense item.

Question 61

Explain the concept of Bonus share.

Answer:

Bonus shares are additional shares given to the current shareholders without any additional cost, based upon the number of shares that a shareholder owns. These are company's accumulated earnings which are not given out in the form of dividends, but are converted into free shares.

Question 62

Discuss the limitations which must be kept in mind while evaluating the Financial Statements.

Answer:

Limitations which must be kept in mind while evaluating the Financial Statements are as follows:

- The factors which may be relevant in assessing the worth of the enterprise don't find place in the accounts as they cannot be measured in terms of money.
- Balance Sheet shows the position of the business on the day of its preparation and not on the future date while the users of the accounts are interested in knowing the position of the business in the near future and also in long run and not for the past date.
- Accounting ignores changes in some money factors like inflation etc.
- There are occasions when accounting principles conflict with each other.
- Certain accounting estimates depend on the sheer personal judgement of the accountant.
- Different accounting policies for the treatment of same item add to the probability of manipulations

Question 63

Explain the second Procedural Aspect of Accounting i.e.Using the financial Information.

Answer:

There are certain users of accounts. Earlier it was viewed that accounting is meant for the proprietor or owner of the business, but changing social relationships diluted the earlier thinking. It is now believed that besides the owner or the management of the business enterprise, users of accounts include the investors, employees, lenders, suppliers, customers, government and other agencies and the public at large, Accounting provides the art of presenting information systematically to the users of accounts. Accounting data is more useful if it stresses economic substance rather than technical form. Information is useless and meaningless unless it is relevantand material to a user's decision. The information should also be free of any biases. The users should understand not only the financial results depicted by the accounting figures, but also should be able to assess its reliability and compare it with information about alternative opportunities and the past experience.

Question 64

List of the different types of users.

Answer:

Internal users

- Board of
- Directors
- Partners
- Managers
- Officers

External users

- Investors
- Lenders
- Suppliers
- Govt. agencies
- Customers

Question 65

What is the uses of the term Transactions &Events?

Answer:

Transaction is used to mean a business, performance of an act, an agreementwhile event is used to mean 'a happening, as a consequence of transaction(s), a result.

Question 66

What do you mean by Fair value?

Answer:

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction.

Question 67

For the concept of Conservatism there should be qualitative characteristics of financial statements State them

Answer:

For this concept there should be at least three qualitative characteristics offinancial statements, namely,

- **Prudence** i.e. judgement about the possible future losses which are to be guarded, as well as gains which are uncertain
- **Neutralit**y i.e. unbiased outlook is required to identify & record such possible losses, as well as to exclude uncertain gains,
- **Faithful r**epresentation of alternative values

Question 68

Differentiate LIFO & FIFO method of inventory.

Answer:

Last in, First Out (LIFO)

Computation of the cost of items sold or consumed during a period on the basis that the items last acquired were sold or consumed first.

First in, First Out (FIFO)

Computation of the cost of items sold or consumed during a period as though they were sold or consumed in order of their acquisition.

Question 69

What are the Objectives of Book Keeping?

Answer:

Complete Recording of Transactions It is concerned with complete and permanent record of all transactions in a systematic and logical manner to show its financial effect on the business.

Ascertainment of Financial Effect on the Business - It is concerned with the combinedeffect of all the transactions made during the accounting period upon the financial positionof the business as a whole

Question 70

Define revenue receipts and give examples. How are these receipts treated?

Answer:

Receipts which are obtained in course of normal business activities are revenue receipts (e.g. receipts from sale of goods or services, interest income etc.). Revenue receipts should not be equated with the actual cash receipts. Revenue receiptsare credited to the Profit and Loss Account.

Question 71

Define the term Historical cost of the Assets.

Answer:

Historical Cost is the original cost incurred in the past to acquire an asset. Historical Cost Convention requires assets to be recognized at their historical cost.

Question 72

A machine was acquired 5 years ago for Rs. 10,000'

New machine with the same specification would cost Rs. 40000 today due to inflation.

The current market value of the machine in its present condition is RS. 6000

Machine is depreciated using straight line basis over its useful life of 10 years

Using the historical cost convention, what would be the net book value of the machine today?

Answer:

Net book value = Cost - Accumulated Depreciation

=Rs. 10,000 - (Rs. 10,000 x 5/10)

=Rs. 5,000

The machine would be assigned a historical cost of Rs. 10,000.

The replacement value (i.e. Rs. 40,000) & fair value (i.e. Rs. 6,000) would not be considered in the valuation

Question 73

What are the benefits of convergence with IFRS?

Answer:

There are many beneficiaries of convergence with IFRS such as the economy, investors, industry etc.

The Economy: When the markets expand globally the need for convergence increases since the convergence benefits the economy by increasing growth of its international business. It facilitates maintenance of orderly and efficient capital markets and also helps to increase the capital formation and thereby economic growth. It encourages international investing and thereby leads to more foreign capital flows tothe country.

Investors: Financial statements prepared using a common set of accounting standards help investors better understand investment opportunities as opposed to financial statements prepared using a different set of national accounting standards. Investors'confidence is strong when accounting standards used are globally accepted. Convergence with IFRS contributes to investors' understanding and confidence in high quality financial statements.

The Industry: A major force in the movement towards convergence has been the interest of the industry. The industry is able to raise capital from foreign markets at lower cost if it can create confidence in the minds of foreign investors that their financial statements comply with globally accepted accounting standards.

Question 74

M/s ABC &Co. Run a restaurant. They renovate some of the old cabins. Because of this renovation some space was made free and number of cabins was increased from 10 to 13. The total expenditure was `20,000. Is these Expenses being Capital in Nature?

Answer:

Renovation of cabins increased the number of cabins. This has an effect on thefuture revenue generating capability of the business. Thus, the renovation expense iscapital expenditure in nature.

Question 75

Name the alternative measurement bases, for determining the value at which an element can be recognized in the balance sheet or statement of profit and loss.

Answer:

Alternative measurement bases are:

- Historical Cost;
- Current cost
- Realizable (Settlement) Value and
- Present Value.

Question 76

What does the Conversion cost of Assets Mean?

Answer:

Cost incurred to convert raw materials or components into finished or semi-finished products. This normally includes costs which are specifically attributable to units of production, i.e., direct labour, direct expenses and subcontracted work, and production overheads as applicable in accordance with either the direct cost or absorption costing method. Production overheads exclude expenses which relate to general administration, finance, selling and distribution.

Question 77

Mr. A, who owns & operates a bookstore, has identified the following transactions for the month of January that need to be accountant for in the monthly financial statements

1. Payment of salary to staff	**Rs. 2000**
2. Sale of books for cash	**RS. 5000**
3. Sales of books on Credit	**Rs. 15000**
4. Receipts from Credit customers	**RS. 10000**
5. Purchase of book for cash	**Rs. 20000**
6. Utility Expenses – unpaid	**Rs. 3000**

Answer:

Under double entry System, the above transactions will be accounted for as follows-

	Debit (Rs)
Credit(Rs)	

1. Salary Expense increase in expenses 2000
2000
Cash at bank decrease in asset

2. Cash in hand increase in asset 5000
5000
Sales Revenue increase in income

3. Receivableincrease in asset 15000 15000
Sales Revenue decrease in income

4. Cash at bank increase in asset 10000 10000
Receivabledecrease in asset

5.Purchasesincrease in expenses 20000 20000
cash at bank decrease in asset

6. Utility expense increase in expenses 3000
3000
Accrued Expenses decrease in asset

Question 78

What are possible indications of going concern problems?

Answer:

Indications of going concern problems

- Deteriorating liquidity position of a company not backed by sufficient financingarrangements.
- High financial risk arising from increased gearing level rendering the company vulnerable to delays in payment of interest and loan principal.
- Significant trading losses being incurred for several years.
- Profitability of a company is essential for its survival in the long term.
- Aggressive growth strategy not backed by sufficient finance which ultimately leads to over trading.
- Increasing level of short-term borrowing and overdraft not supported by increase inbusiness.

- Inability of the company to maintain liquidity ratios as defined in the loan covenants. Serious litigations faced by a company which does not have the financial strength to paythe possible settlement.
- Inability of a company to develop a new range of commercially successful products.
- Innovation is often said to be the key to the long-term stability of any company Bankruptcy of a major customer of the company.

Question 79

Define Money Measurement Concept with Recognition Criteria.

Answer:

Money Measurement Concept in accounting, also known as Measurability Concept means that only transactions and events that are capable of being measured in monetary terms are recognized in the financial statements. The recognition criteria require that the elements of financial statements (i.e., assets, liabilities, income and expense) must only be recognized in the financial statements if its cost or value can be measured with sufficient reliability. Therefore, an entity shall not recognize an element of financial statement unless a reliable value can be assigned to it.

Question 80

Define the Term Current Assets & Current Liability.

Answer:

Current Assets

Cash and other assets that are expected to be converted into cash or consumed in the production of goods or rendering of services in the normal course of business.

Current Liability

Liability including loans, deposits and bank overdraft which falls due for payment in a relatively short period, normally not more than twelve months.

Question 81

What is Accounting Concepts.? Explain

Answer:

Accounting concepts define the assumptions on the basis of which financial statements of a business entity are prepared. Certain concepts are perceived, assumed and accepted in accounting to provide a unifying structure and internal logic to accounting process. The word concept means idea or notion, which has universal application. Financial transactions are interpreted in the light of the concepts, which govern accounting methods. Concepts are those basic assumptions and conditions, which form the basis upon which the accountancy has been laid. Unlike physical science, accounting concepts are only result of broad consensus. These accounting concepts lay the foundation on the basis of which the accounting principles are formulated.

Question 82

What does Ind-As mean for? Explain in Brief.

Answer:

Indian Accounting Standards (Ind-AS) are the International Financial Reporting Standards (IFRS) converged standards issued by the Central Government of India under the supervision and control of Accounting Standards Board (ASB) of ICAIand in consultation with National Advisory Committee on Accounting Standards (NACAS)

National Advisory Committee on Accounting Standards (NACAS) recommend these standards to the Ministry of Corporate Affairs (MCA), MCA has to spell out the accounting standards applicable for companies in India.

The Ind AS are named and numbered in the same way as the corresponding International Financial Reporting Standards (IFRS).

Question 83

Explain key Characteristics of Accounting Information.

Answer:

There is general agreement that, before it can be regarded as useful in satisfying the needs of various user groups, accounting information should satisfy the following criteria:

Understandability

This implies the expression, with clarity, of accounting information in such a way that itwill be understandable to users - who are generally assumed to have a reasonable knowledge of business and economic activities

Relevance

This implies that, to be useful, accounting information must assist a user to form, confirm or maybe revise a view - usually in the context of making a decision (e.g., should I invest, should I lend money to this business? Should I work for this business?)

Consistency
This implies consistent treatment of similar items and application of accounting policies

Comparability
This implies the ability for users to be able to compare similar companies in the same industry group and to make comparisons of performance over time. Much of the work that goes into setting accounting standards is based a "neutral" way. In other words, it is not biased towards a particular user group or vested interest around the need forcomparability

Reliability
This implies that the accounting information that is presented is truthful, accurate, complete (nothing significant missed out) and capable of being verified (e.g. by a potential investor).

Objectivity
This implies that accounting information is prepared and reported in

Question 84
Do you think Accounting Standards are mandatory and why?
Answer:
Yes, I do believe that accounting standards play a very important role to prepare good quality and accurate financial reports. It ensures reliability and relevance in financial reports.

Question 85
Can you name different branches of accounting?
Answer:
There are three branches of accounting named as "Financial Accounting". "Management Accounting" and "Cost Accounting".

Question 86
Mention the types of accounts involved in double entry book-

keeping?

Answer:

Double entry book-keeping involves five types of accounts,

- Income accounts
- Expense accounts
- Asset accounts
- Liability accounts
- Capital accounts

Question 87

Explain what is the difference between accumulated depreciation and depreciation expense?

Answer:

The difference between accumulated depreciation and depreciation expense is thatAccumulated depreciation: It is the total amount of depreciation that has been taken on a company's assets up to the date of the balance sheet Depreciation expense: It is the amount of depreciation that is reported on the income statement. Basically, it is the amount that corresponds only to the period of time indicated in the heading of the income statement,

Question 88

Mention what does financial statement of the company includes?

Answer:

Financial statement of the company includes various information like

- Balance Sheet (Assets, liabilities, and equity)
- Income statement (Profit or Loss statement)
- Equity statement Cash flow statement

Question 89

Mention in simple terms what is the difference between Asset, equity, and liabilities?

Answer:

- **Asset**: What financial institute (bank) or people owe you
- **Liabilities**: It is something you owe people or organization
- **Equity**: It is something you own, for example, the amount of your house loan you paid off

Question 90

Define Cost Accounting.

Answer:

Cost Accounting - The terminology of Cost Accounting published by the Institute of Cost and Management Accountants of England defines cost accounting as: "the process of accounting for cost which begins with the recording of income and expenditure or the bases on which they are calculated and ends with the preparation of periodical statements and reports for ascertaining and controlling costs."

Question 91

Differentiate Accrued assets & Accrued Expenses

Answer:

Accrued Asset

A developing but not yet enforceable claim against another person which accumulates with the passage of time or the rendering of service or otherwise. It may arise from the rendering of services (including the use of money) which at the date of accounting have been partly performed, and are not yet billable.

AccruedExpense

An expense which has been incurred in an accounting period but for which no enforceable claim has become due in that period against the enterprise. It may arise from the purchase of services (including the use of money) which at the date of accounting have been only partly performed, and are not yet billable.

Question 92

Explain the relevance of selection of accounting policies.

Answer:

Choice of accounting policy is an important policy decision which affects theperformance measurement as well as financial position of the business entity. Selection of inappropriate accounting policy may lead to understatement or overstatement of performance and financial position. Thus, accounting policy should be selected with due care after considering its effect on the financial performance of the business enterprise from the angle of various users of accounts.

Examples wherein selection from a set of accounting policies is made, can be given asfollows:

- Inventories are valued at cost except for finished goods and by-products. Finished goods are valued at lower of cost or market value and by-products are valued at net realizable value.
- Investments (long term) are valued at their acquisition cost. Provision for permanent diminution in value has been made wherever necessary.

Question 93

What is mean by Recurring &non-recurring nature of Expenses.

Answer:

If the frequency of an expense is quite often in an accounting year then it is saidto be an expenditure of revenue nature while non-recurring expenditure is infrequent in nature and do not occur often in an accounting year.

Past Examination Questions

MAY 2018

Question 1

State with reasons, whether the following statement is true or false: Expenses in connection with obtaining a license for running Cinema Hall is Revenue Expenditure

Answer:

False: Licence for running the Cinema house is necessary, hence its cost should be capitalised. This is an item of expenditure incurred to acquire the right to carry on business.

Question 2

Differentiate between Provision and Contingent liability.

Answer:

Provision	Contingent liability
Provision is accounted for at present as a result of a past event.	Contingent liability is recorded at present to account for a possible future outflow of funds.

The occurrence of provisions is certain.	The occurrence of contingent liability is conditional.
The amount of provision is largely not certain.	A reasonable estimate can be made for the amount of payment.
Provision is recorded as a decrease in assets in Statement of financial position.	Contingent liability is recorded as an increase in liabilities in Statement of financial position
Increase or decrease of provisions is recorded in the Income statement.	Contingent liability is not recorded in the Income statement.

NOVEMBER 2018

Question 3

State with reasons. Whether the following statement is true or false: Overhauling expenses for the engine of motor car to get better fuel efficiency is revenue expenditure

Answer:

False– Overhauling expenses are incurred for the engine of a motor car derive better fuel efficiency. These expenses will reduce the running cost in future and thus the benefit is in form of endurable long – term advantages, so that expenditure should be capitalised.

MAY 2019

Question 4

State with reason, whether the following statements are true or false amount spent for the construction of temporary huts, which were necessary for construction of the cinema house and were demolished when the cinema house was ready, is capital expenditure

Answer:

True: - Any expenditure incurred which Is related to capital expenditure is part of it so added to its cost. As construction of temporary huts were necessary for the construction of the cinema house is there by part of capital expenditure

Question 5

Distinguish between going concern concept & cost concept.

Answer:

Going Concern	Cost Concept
1. As per this concept business will go on far ever i.e., far at least foreseeable future	1. As per this concept every transaction is recorded at cost i.e. what amount paid for the transaction.
2. Going concern is one of the fundamental accounting assumptions	2. It is not a fundamental accounting assumption but an accounting concept.
3. For every business organization formed for long term, going concern assumption is must.	3. Due to revaluation concept some business may or may not follow cost concept

NOVEMBER 19

Question 6

Briefly explain the differences between the following:

(a) Contingent liability and other liabilities [5 Marks]

Answer:

Contingent liability & other liabilities: Liability is defined as the financial obligation of an enterprise other than owner's fund. They may be classified into current liabilities and long – term liabilities. Creditors, bills payable and outstanding expenses are examples of current liability whereas debentures and term loans from banks and financial institutions are examples of long-term liabilities.

Guidance note on terms used in financial statements defines contingent liabilities as an obligation relating to an existing condition or situation which may arise in future depending on the occurrence or non-occurrence of one or more uncertain future events. Contingent liabilities may be in respect of bills discounted, pending suits etc. Thus, it is not an actual liability and as such it is not recorded in the balance sheet. It is simply mentioned by way of foot note to the balance sheet.

Question 7

M/s. XYZ & Co. runs a café. They renovated some of the old cabins. Because of this renovation some space was made free and number of cabins was increased from 15 to 18. The total expenditure incurred was 30,000 and was treated as a revenue expenditure.

Answer:

False: Renovation of cabins increased the number of cabins. This has an effect on the future revenue generating capability of the business. Thus, the renovation expense iscapital expenditure in nature.

DEC 2020

Question 8

State with reasons, whether the following statement are True or False:

I. **In the balance sheet of X Limited preliminary expenses accounting Rs. 5 lakhs and securities premium account of Rs 35 lakh are appearing the account can use the balance in securities premium account. To write off preliminary expenses.**

Answer:

True: According to section 52 of the companies Act 2013, securities premium Account may be used by the company to write of preliminary Expenses of the company.

II. **Insurance claim received on account of plant and machinery completely damaged by fire is a capital receipt.**

Answer:

True: Insurance claim received is not normal Business Activities and hence it is capital receipt.

Question 9

What services can a Chartered Accountant provide to the society?

Answer:

a. Taxation
b. Legal services
c. Auditing
d. financial management
e. Financial Analysis
f. Investment Decisions
g. cost Accounting
h. cost Accounting

Question 10

Max & Co. employs a team of 9 worker who were paid Rs. 40,000 per month each in the year ending 31st December, 2018 At the start of 2019 the company raised salaries by 10% to Rs. 44,000 per month each.
On 1st July 2019 the company hired 2 trainees at salary of Rs. 21000 per month each The work force are paid salary on the first working day of every month one month in arrears so that the employee receive their salary for January on the first working day of February etc.

You are required to calculate:

I. **Amount of salaries which would be charged to the profits and loss for the year ended 31st December, 2019**
II. **Amount actually paid salaries during 2019**
III. **Outstanding salaries as on 31st December, 2019**

Answer:

The books of Max & co. In

Calculation of Amount of salaries to be charged in p/L a/c for the year ended 31-Dec-2019

A. Salaries of 9 weaker @ 44000 /- per Month 4752000
(9× 44000 ×12)
B. Salaries of 2 Trainees @ 21000 per month 252000
(2× 210000 × 6 Month)
Amt of salaries to be charged In P/L 5004000.

(i) **Amount actually paid as salaries during 2019**
a. Dec. 2018
salaries (9×40000) = 360000

b. From 1/Feb./ 2019 to 1 /Dec/ 2019
salaries of 9 worker of 11 month = 4356000
(9 × 44000 × 11)

c. From 1/ Feb./ 2019 to 1/ dec/2019
Salaries of 2 trainee for 5 months =210000
(2 × 21000 × 5)
Total **4926000**

(ii) Outstanding salaries as on 31/ Dec / 2019

a. Salaries of 9 worker for 1 month 396000
(9 ×44000)
b. Salaries of 2 trainee for 1 month 42000
(2 × 21000)
Total 438000

Jan 2021

Question 11

Subsidy received from the government for working capital by a manufacturing is a revenue receipt.

Answer:

TRUE:Any amount received on operating activities of business is a revenue receipt hence subsidy received from the government for working capital by a manufacturing concern is a revenue receipt.

Question 12

Consignee will not post any journal entry in his books at time of receiving of goods from Consigner

Answer:

TRUE: In the books of consignee no entry is require to be passed at the time of receiving goods from consignor

Question 13

Accounting standards for non-corporate entities in India are issued by the

Central Government

Answer:

FALSE: Accounting standards for non-corporate entities in India are issued by the ICAI not by the government.

Question 14

Define the followings terms

I. **Capital Commitment**

Answer:

CAPITAL COMMITMENT: Future liability for capital expenditure in respect of which contracts have been made.

II. **Expired Cost**

Answer:

EXPIRED COST: That position of an expenditure from which no further benefit is expected. Also termed as expense.

III. **Obsolescence**

Answer:

Diminution in the value of an asset by reason of its becoming out-of-date or less useful due to technological changes improvement in production methods, change in market demand for the product or service output of the asset, or legal or other restrictions.

JULY 2021

Question 15

Discuss the basic consideration is distinguishing between capital and revenue expenditure.

Answer:

The basic consideration in distinction between capital and revenue expenditure are:

a) **Nature of business:** For a trader dealing in furniture, purchase of furniture is revenue expenditure but for any other trade, the purchase of furniture should be treated as capital expenditure and show in the balance sheet as asset.

b) **Recurring nature of expenditure:** If the frequency of an expense is quite often is an accounting year, then it is said to be an expenditure of revenue nature while non-recurring expenditure is infrequent in nature and do not occur often in an accounting year.

c) **Purpose of expenses:** Expenses for repair of machine may be incurred in course of normal maintenance of the asset. Such expenses are revenue in nature. On the other hand, expenditure incurred for major repair of the asset so as to increase its productive capacity is capital in nature.

d) **Effective on revenue generating capacity of business:** The expenses which help to generate income/ revenue in the current period are revenue in nature and should be matched against the revenue earned in the current period. On the other hand, if expenditure helps to generate revenue over more than one accounting period, it is generally called capital expenditure.

e) **Materiality of the amount involved:** Relative proportion of the amount involved is another important consideration in distinction between revenue and capital.

DEC 2021

Question 1

State with reasons, whether the following statements are True or False:

(i) **Any amount spent to minimize the working expenses is revenue expenditure.**

(ii) **Expenses incurred on the repairs for the first time on purchase of an old building are capital expenditure.**

(iii) **The provision for bad debts is debited to sundry debtors account.**

Answer:

i. **False:** It may be reasonably presumed that money spent for reducing revenue expenditure would have generated long-term benefits to the entity. So this is capital expenditure.

ii. **True:** Repairs for the first time of an old building are incurred to put the building in usable condition. This is a part of the cost of building. Accordingly, this is a capital expenditure.

iii. **False:** The provision for bad debts is debited to Profit and loss Account, in Balance Sheet it is shown either on liability side or deducted from the head debtors.

Question 2

Explain the followings:

(i) Accrual Basis of Accounting

(ii) Amortisation

(iii) Contingent Assets

(iv) Contingent Liabilities

Answer:

(i) Accrual Basis of Accounting

The method of recording transactions by which revenues, costs, assets and liabilities are reflected in the accounts in the period in which they accrue.

(ii) Amortisation

The gradual and systematic writing off of an asset or an account over an appropriate period.

(iii)Contingent Asset

An asset the existence, ownership or value of which may be known or determined only on the occurrence or non-occurrence of one or more uncertain future events.

(iv)Contingent Liability

An obligation relating to an existing condition or situation which may arise in future depending on the occurrence or non-occurrence of one or more uncertain future events.

JUNE 2022

Question 1

State with reasons, whether the following statements are True or False:

(i) **A claim that an enterprise is pursuing through legal process, where the outcome is uncertain, is a Contingent Liability.**

(ii) **Any amount spent for replacement of worn out part of a machine is capital expenditure**

Answer:

i. False: A claim that an enterprise is pursuing through legal process, where the outcome is uncertain, is a contingent asset.

ii. False: Amount spent for replacement of any worn- out part of a machine is revenue expense since it is part of its maintenance cost

DEC 2022

Question 1

State with reasons, whether the following statements are True or False:

i. **The provision for discount on creditors is often not provided in keeping with the principle of conservatism.**

ii. **Both revenue and capital nature transaction are recorded in the receipts and payments Account.**

Answer:

i. **True –** According to the principle of conservation provision is maintained for the losses to be incurred in future. Discount on creditors is on Income so provision is not maintained.

ii. **True-** Receipt and Payment account records both revenues and capital nature transactions.

Question 2

Differentiate between Provision and Contingent Liabilities.

Answer:

The main differences between Provision and Contingent Liabilities are as follows:

Provision Liability	Contingent Liability
Definition	
Provision liability reduces an asset's value because of a present obligation arising out of a past event.	Contingent liability is a potential liability that can occur at a future date due to events beyond a company's control.
Certainty of the event	
The event which can result in a provisional liability may or may not occur.	The event which can result in a contingent liability will occur.
Estimate of the liability	
The estimated amount of the provisional liability is not certain.	The estimated amount of the contingent liability is largely certain.
Profit and Loss Account	
Any increase or decrease in provision liability gets recorded in the Profit and Loss Account.	The Profit and Loss Account does not record a contingent liability.
Examples	

Some of the examples of a provision liability are as follows: • Provision for bad debts • Provision for doubtful debts	Some of the examples of a contingent liability are as follows: • Product warranties • Outstanding Lawsuits • Pending Investigations • Debts

Question 3

''The cost of property, Plant and Equipment comprises of any cost directly attributable to bring the asset to the location and condition necessary for it to be capable of operating in a manner intended by the enterprise''. Give any five examples of such 'directly attributes costs'.

Answer:

Cost of property, plant and equipment ('PP&E') comprises (IAS 16.16):

- **a)** Purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
- **b)** Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
- **c)** The initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Examples of directly attributable costs include:

- labour expense (as per IAS 19) resulting from the construction or acquisition of an asset,
- direct materials used,
- systematic allocation of variable and fixed production overheads,
- delivery costs,
- site inspection and preparation,
- installation,
- costs of testing whether the asset is functioning properly,
- Professional fees (e.g. legal fees, stamp duty).