Chapter-1

Introduction to Accounting

Accounting is the language of business. It is the systematic process of identifying, recording, classifying, summarising, interpreting and communicating financial information to users. Accounting shows the profit earned or loss incurred during the accounting period. It also displays the value and nature of assets, liabilities and capital. The primary objective of accounting is to provide accounting information to interested parties to facilitate right business decisions.

Definition

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

Economic Events

Business is an economic activity. Economic activities are performed through transactions and events (Outcome of transactions).

Lots of economic events takes place in a business organisation. An event is the outcome of certain transactions, which are measurable in terms of money. All the events which can be measured in terms of money are classified as **economic events** and are recorded in the financial statements.

A business has earned a profit of Rs. 10,000. It is the result/ outcome of certain transactions that takes place in a business. It is an economic event because its value can be measurable in terms of money. Appointment of an efficient manager, change in fashion etc. ate events but its can not be measurable in terms of money.

Example :1

Mr.Rajan, a sole trader invested Rs.3,00,000 to start s stationery shop. On 1-09-2020 he purchased goods worth Rs.1,80,000 and sold it for Rs.2,00,000 during the month September 2020.He paid Rs.7,000 as rent for the month. Everything Rajan does is part of a business. Rajan naturally wants to know the result of his business activities. Accounting helps the business people with this.

		Rs.
Goods Sold		**2,00,000**
Less: Goods Purchased	**1,80,000**	
Rent Paid	**7,000**	**(1,87,000)**
Surplus		**13,000**

In the above example, there are different types of transactions takes place, for example, capital contributed by the owner into the business, purchase and sales of goods and rent paid. The outcome (event) of the above transactions: (1) Earned a profit of Rs.13,000

Accounting is responsible for identifying and recording all business transactions. Accounting provides useful information to managers and other users of accounting information's to take right decisions on time.

Business Transaction

A business transaction is an event involving an interchange of goods, money or services between two or more entities. In a business transaction there should be two entities. Its value should be measurable in terms of money. A transaction is a two-way process in which value is transferred from one party to another.

For example, purchased goods from Mohan Traders worth Rs.5,000 for cash, here cash Rs. 5,000 transferred from business to Mohan Traders and at the same time business received goods worth Rs.5000 from Mohan Traders.

A transaction may be **external or internal.**

1.External Transactions

Transaction between an outsider and an organisation is called external transactions. The following are the examples of such transactions:

- Purchased goods from suppliers
- Sold goods to customers
- Rent paid to building owner
- Electricity expenses paid

2. Internal Transactions

An internal transaction is one that occurs entirely between the internal wings of an enterprise.

- Supply of raw materials from stores department to the production department.

Characteristics/ Nature/ Features of Accounting

The above definition contains four essential characteristics of accounting:

1. **Identifying and Recording Business Transactions (Economic Events only)**

Business transactions are economic events that affect a business's financial position. Accounting can only record those transactions that are valued in the form of money. Business transactions are recorded by using monetary unit, viz. rupees and paise as a measuring unit. If an event cannot be quantified in monetary terms, it is not considered for recording in financial accounts. The recording is done in a book called ***Journal*.**

*(There are also some events takes place in business which are also very important for the business too but which **cannot be measured in terms of money.** For example appointment of an efficient manager, death of an efficient employee etc. Effect of such events can't be measured in terms of money, so it **cannot be recorded**.)*

Example for business transaction / Economic Events	Example for Non-Economic Events
Commenced business with cash	Quarrel between Purchase manager and Production manager
Goods purchased on credit	Resignation of an able and experienced manager
Salary paid	Strike by employees
Withdraw cash for personal use	Starting of a new business by the competitor

Note: Non economic events can't be recorded in the books of accounts.

2. **Classifying**
   After recording the transactions in subsidiary book or journal proper, the transactions are to be classified. Classification is the systematic analysis of the recorded data with a view to bringing together items of a similar nature at one place (Account). The classification work is done in the book called **Ledger**, where various types of accounts are maintained.
3. **Summarising**
   This involves presenting the classified data in a manner which is understandable and useful for internal as well as external users of accounting system.Summarising leads to the preparation of the following statements:
   - Trial Balance
   - Trading and Profit and Loss Account
   - Balance Sheet
4. **Analysis and interpretation**
   The financial data recorded is analysed and interpreted in such a manner that the end-users can make a meaningful judgment about the profitability and financial condition of the business.
5. **Communicating**
   Finally, accounting involves communicating financial data to its users. Users includes owners, managers, employees, investors creditors etc. The accounting information should be communicated to the right person at the right tine to take right decision.

   Note:
   The process of accounting starts with identifying transactions and ends with communicating information.

Need for accounting

At the end of an accounting year every businessman wants to know how much profit the business made last year. Further the owner wants to know the financial position of the business. In order to ascertain such information, it is essential to keep a complete and systematic record of each and every business transaction occurred during the year.

Objectives of Accounting

Main objectives/functions of accounting are:

1. **Maintaining Accounting records**
   The main objective of accounting is to maintain systematic record of business transactions and events. Business transactions are recorded in books of account in monetary terms and in a chronological order.
2. **Ascertainment of result**
   The second objective of accounting is to ascertain the net profit earned or loss suffered on account of business transactions during a particular year. For this purpose a statement called 'Income statement' or 'Trading and profit and Loss Account' is prepared.
   Trading and Profit and Loss Account provides the following information:
   - How much goods have been purchased during a particular year?
   - How much goods have been sold during a particular year?
   - How much goods have remained unsold and what is it value?
   - How much amount has been spent on various heads of expenditure?
   - How much amount has been earned by various heads of revenue?
3. **Determining the Financial Position**
   The business man also knows the financial position of the business. For this purpose, a statement called 'Balance Sheet' is prepared, it shows the various assets and its values on the one hand and the liabilities and capital on the other hand.
4. **Provide Information to Various Parties**
   Accounting as a 'language of business' communicates the relevant accounting information to various interested parties. owners, investors, creditors, banks, employees and Government. The information helps them in taking sound and judicious decisions about the business entity.

Users of Accounting Information	
Internal Users (Parties within the business organization)	**External Users** (Parties outside the business organization)
Owners	Investors (shareholders), banks
Managers	Creditors (Banks, financial institutions, debenture holders, other lenders)
Employees	Government authorities
	Trade Unions
	Stock Exchange, SEBI, Registrar of Companies
	Researchers
	Consumers
	General public

5. **Meeting Legal Requirements**
   Accounting records are accepted as evidence by the court, if they are maintained systematically. Besides, the law such as Companies Act, Income Tax Act, GST Act etc. requires timely submission of returns.
6. **Assistance to Management**
   Management often requires financial information for decision making and ensures efficient management. By providing timely information, accounting assists the management in the task of planning, controlling and decision making.

Functions of Accounting

Th main functions of accounting are:

1. **Measurement:** Accounting measures past performance of the business entity and display its current financial position.

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

3. **Decision making**: Accounting provides relevant information to the users of accounts to take correct decisions.

4. **Comparison and Evaluation**: Accounting assess performance achieved in relation to target and provide necessary information to managers.

Advantages/ Importance of Accounting

1. Accounting **keeps** a prompt and **systematic record** of all transactions.
2. Accounting **helps** the management in **taking business decisions** by analyzing the financial statements and other information.
3. Accounting **reports net result of business** activities of an accounting period by preparing Trading profit and loss account.
4. Accounting **reports the financial position** of the business by preparing a Balance Sheet at the end of the accounting period.
5. It facilitates comparative study of the performance of the business over different periods of time and with other firms.
6. Court accepts these records as evidence in case of disputes.

Limitations of Accounting

1. **Recording past events**
   Accounting is historical in nature, i.e. what has happened in the past. From the decision-making view point, information is needed not only of past but also about the present and the future.
2. **Recording only monetary items**
   It records only transactions which can be recorded in monetary terms. Qualitative aspects like managerial skills, services of experts, satisfaction level of firm's customers etc. are not recorded.
3. **Application of different methods**
   Use of different accounting methods by different firms reduces the reliability of accounts.

Accounting Process

In a business there are numerous transactions will take place. It is impossible for the business man to keep a memory of entire transactions of business. There must be documentary evidence of every financial transaction. Business transactions like purchase of goods, sale of goods, payment of wages etc. have an effect on the assets, liabilities and capital of the business. We can ascertain the result of the business in terms of profit/loss and value of assets and liabilities, if we maintain systematic and scientific record (Accounting) of all the transaction of financial nature. Accounting process can be briefly explained as follows:

Step-1 Identifying business transaction is the first step of accounting. These transactions are recorded in the subsidiary books and journal proper.

Step-2 With the help of subsidiary book we can prepare Ledger accounts.

Step-3 The balances shown by ledger accounts are used for preparing Trial Balance, which serves as the basis for the preparation of financial statements.

Step-4 Preparation of Financial Statement-Financial statement is classified as Income Statement and Position Statement.

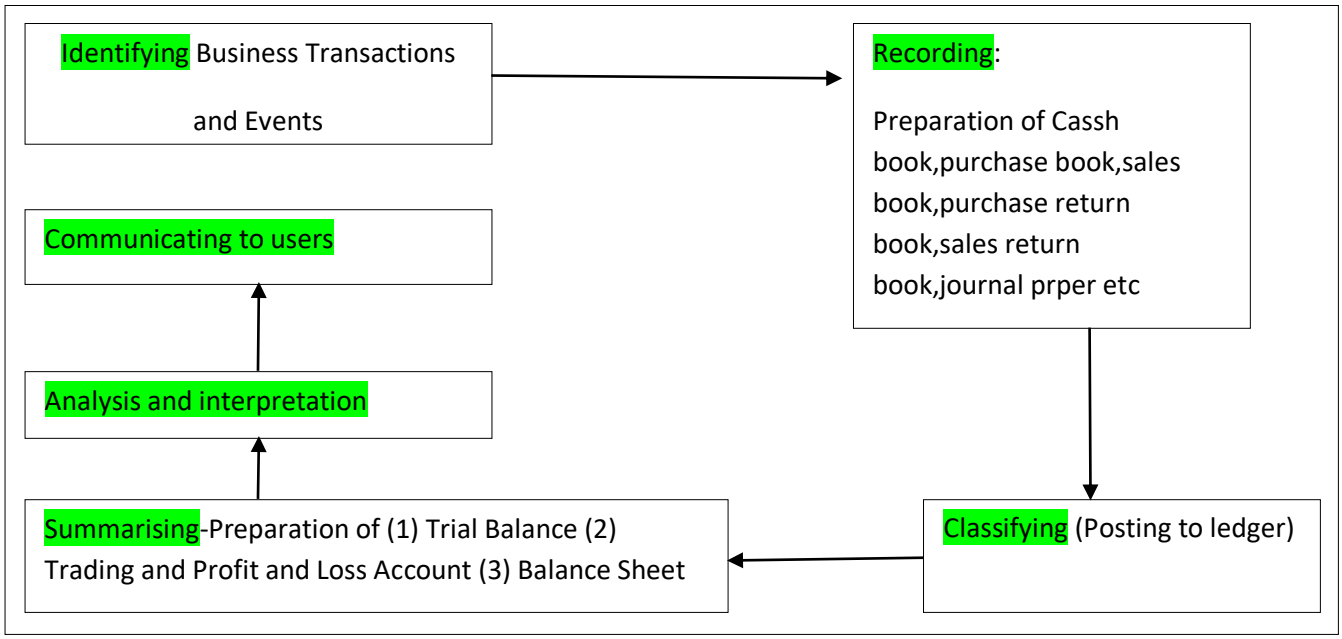
Income statement consists of Trading account which shows Gross Profit/Loss and Profit and Loss Account, which shows Net Profit/Loss.

Finally, Position statement (Balance Sheet) is prepared, which reflects the true position of assets and liabilities of the business.

Step-5 Analysis of financial statements and report it to various parties. The information helps them in taking sound and judicious decisions about the business entity.

Step-6 Communicating -It is concerned with the transmission of summarized, analysed and interpreted information to the end-users to enable theme to make rational decisions.

Accounting Process-Diagrammatic presentation



Book-Keeping, Accounting and Accountancy

The terms 'Book Keeping and 'Acccounting', often considered as same, but it is not correct. Accounting is a wider concept and includes book keeping also.

Book-keeping

According to JR Batliboi"Book-keeping is an art of recording business dealings in a set of books"

Book keeping is a part of accounting and it is mainly concerned with recording transactions in the journal, classifying and summarizing them into accounts through posting, balancing of accounts and preparation of a trial balance.

Accounting

Accountant's work goes beyond that of a book-keeper. **Accounting starts where book-keeping ends**. It includes the following activities:

1) **Summarising**-Summarising the classified information in the form of Profit and Loss Account and Balance Sheet
2) **Analysing and interpreting**-after reading and analyzing profit and loss account and balance sheet, accountant find out or drawing out meaningful information from them.
3) **Communication**-Here accountant communicate relevant information s to interested parties.

In actual practice the accounting process includes the book-keeping functions also because on the basis of book-keeping records ,an accountant prepare financial statements like Profit and Loss Account, Balance Sheet etc.In a small concern, the accountant performs the work of book-keeper also.

Difference between Book-keeping and Accounting

Basis	Book Keeping	Accounting
Stage	It is the primary stage and act as the base for accounting.	Accounting begins where book-keeping ends.
Decision making	Never helps management in taking decisions.	Decision making possible on the basis of accounting records
Books prepared	Journal and Ledger	Profit and Loss Account, Balance Sheet and Cash Flow Statement
Scope	Just maintains records of business transactions	Preparation of financial statements, interpreting results and communicating it to interested parties
Sub Fields	Single entry system and double entry system of book keeping	Financial accounting, cost accounting, management accounting, human resource accounting
Nature	Book-keeping work is routine and clerical in nature	The accounting work is analytical in nature.

Accountancy

Accountancy refers to a systematic knowledge of accounting. It tells how to prepare books of accounts, its principles, techniques etc. It is a discipline just like physics, chemistry etc. It gives knowledge of how to make accounting works. It is concerned with book-keeping as well as accounting.
According to Kohler “Accountancy refers to the entire body of the theory and practice of accounting”

Branches (Sub-disciplines) of Accounting

1. **Financial accounting**

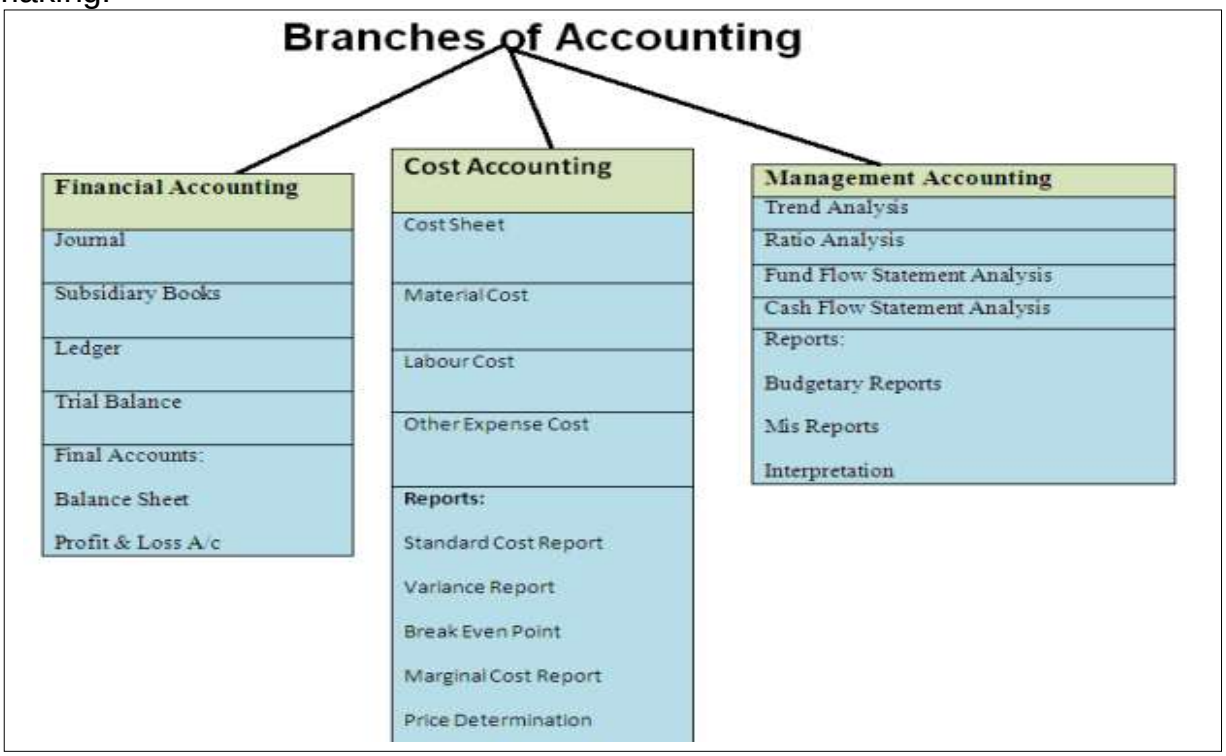
It is the original form of accounting. The object of financial accounting is to find out the result of operation (profit/loss) and to disclose information about the financial position (Strength/weakness) of the business. It also provides financial information to the management and other interested parties.

2. Cost accounting

This branch of accounting is concerned with ascertaining cost of products, operations; process etc.The purpose of cost accounting is to analyse the expenditure so as to ascertain the cost of various products manufactured by the firm and fix the prices. It also helps in controlling the costs and providing necessary costing information to management for decision-making.

3. Management Accounting

It is concerned with generating accounting information relating to funds, costs, profits etc. The main purpose of management accounting is to present the accounting information in such a way as to assist the management in planning and controlling the operations of a business. Management accounting uses various techniques like ratio analysis, budgetary control, fund flow statement, cash flow statement etc. to make the accounting data more useful for managerial decision making.



Accounting as a Source of Information

Every step in the process of accounting generates information. Accounting process begins with the identification of transactions and ends with the preparation of financial statements. Generation of information is not an end in itself. It is a means to facilitate the dissemination of information among different user groups.

Accounting information should ensure to:

• provide information for making economic decisions;

• serve the users who rely on financial statements as their principal source of information;

• provide information useful for predicting and evaluating the amount, timing and uncertainty of potential cash-flows;

Qualitative Characteristics of Accounting Information

Accounting information should be prepared and presented in such a way that it should be useful to the end users and should possess the following qualitative characteristics.

1. Reliability

Accounting information must be reliable. Reliability means the users must be able to depend on accounting information. Reliable information should be free from error and bias and verifiable.Varifiability means it can be verified from the source documents such as cash memos, purchase invoices, sales invoices, agreements, property deed etc.Varifiability ensures the truthfulness of the recorded transactions.

2. Relevance

Relevance refers to how helpful the information is for financial decision-making processes. For accounting information to be relevant, it must possess:

1. *Confirmatory value* – Provides information about past events
2. *Predictive value* – Provides predictive power regarding possible future events

Therefore, accounting information is relevant if it can provide helpful information about past events and help in predicting future events or in taking action to deal with possible future events.

3. Understandability

Accounting information should be recorded, presented and interpreted in such a way that it should be easily understood and grasped by its users. Understandability means decision-makers must interpret accounting information in the same sense as it is prepared and conveyed to them.

4. Comparability

Comparability means that the users should be able to compare the accounting information of an enterprise of the period either with that of other periods (Intra-firm comparison) or with the accounting information of other enterprises (Inter-firm comparison).

Different Roles of accounting

As a language – it is considered as the language of business which is used to communicate information on enterprises.

As a historical record- it is viewed as chronological record of all financial transactions of an organisation at actual amounts involved;

As current economic reality- it is viewed as the means of determining the true income of an entity namely the change of wealth over time;

As an information system – it is viewed as a process that links an information source (the accountant) to a set of receivers (external users) by means of a channel of communication;

Basic Terms in Accounting

Entity

Entity means a reality that has a definite individual existence. Business entity means a specifically identifiable business enterprise like Wipro, Reliance Industries Ltd, ITC Limited, Kalyan Silks etc. An accounting system is always devised for a specific business entity (also called accounting entity)

Business Transaction

A business transaction is an event involving an interchange of goods, money or services between two or more entities. In a business transaction there should be two entities. Its value should be measurable in terms of money. A transaction is a two-way process in which value is transferred from one party to another.

It can be transactions like purchase of goods, receipt of money, payment to a creditor, incurring expenses; etc. It is a financial event expressed in terms of money which brings a change in the financial position of an enterprise. Business transaction may be a **cash transaction** or a **credit transaction**.

Examples:

- Purchased goods worth Rs 2000 from Rajan.
- Sold goods for cash Rs.5000
- Salary paid Rs.10,000
- Furniture purchased from A Ltd Rs.8000
- Anil started business with cash Rs.60,000

Features of business transactions

- It is concerned with money or money's worth
- It brings about a change in the financial position (i.e in Assets, liabilities or capital)
- Every transaction has dual aspects-Receiving (Debit) aspect and Giving (Credit) aspect
- After each transaction, the total assets of a business must be equal to its total liabilities and capital (Always ,ASSET= CAPITAL + LIABILITIES).Therefore ,the equality of the Balance Sheet cannot be disturbed by any transaction.

Assets

Assets are material things or possessions or properties of the business including the amounts due to it from others. Assets help to generate income.

- Physical properties include assets like land and building, furniture, motor car, cash, stock etc.owned by a business.
- Rights in certain things called intangible assets such as goodwill, patents, trademarks etc possessed by the business.
- Amount due to the business from others like debtors, bills recevables,accrued income etc

Example:

Land and building, Plant and machinery, cash and bank balance, stock, bills receivable, money owing by debtors etc.

Assets can be classified into the following categories

1. Non-current Assets

2. Current Assets

3. Fictitious Assets

1. Non –Current Assets

Non-current asset refers to those assets which are held for continued use in the business for the purpose of producing goods or services and are not meant for sale. Non-current assets are held by the business from a long-term point of view.

Example-Fixed assets like Land and building, plant and machinery, furniture, computer, motor vehicles and long-term investment

Non-current assets are further classified into:

(a) Tangible assets

Tangible assets are those assets which have physical existence, i.e., they can be seen and touched.

Example: Land, building, machinery, furniture etc.

(b) Intangible assets

Intangible assets are those assets which do not have physical existence i.e., they cannot be seen and touched.

Example: Patents, good will, trademarks, computer software, prepaid expenses etc.

Like tangible assets, intangible assets also help to generate income to the firm. For example, with the help of Patents businessman is able to produce goods and his goodwill helps in attracting customers easily.

2. Current Assets

Current assets are those assets which are meant for sale or which can be converted into cash within a year. For example, goods are purchased with a purpose to resell and earn profit, debtors can be converted into cash within a short period.

Example-Debtors, stock, bills receivable, cash in hand and cash at bank

3. Fictitious Assets

Fictitious assets are neither tangible assets nor intangible assets. They are losses not written off in the year in which they are incurred but in more than one accounting period.

Example- heavy advertisement expenditure, discount on issue of debentures

Note:

Wasting Asset:

Assets, whose value goes on declining with the passage of time, are known as wasting assets. Example Mines, patents, assets taken on lease etc.

Liabilities

It refers to the amount which the firm owes to outsiders. They represent creditors' claims on the firm's assets.

Liabilities =Assets – Capital

Example-Creditors, Bills Payable, Salary outstanding, Loan from bank

Both small and big businesses find it necessary to borrow money from bank at one time or the other, and to purchase goods on credit from suppliers.

Liabilities can be classified into two:

1. Current Liabilities
2. Non-Current Liabilities

1. Current Liabilities (Short term liabilities)

Current liabilities refer to those liabilities which are to be paid within 12 months from the end of the accounting period.

Example-Creditors, bank overdraft, bills payable, outstanding expenses, short term loans etc.

2. Non-Current Liabilities (Long term liabilities)

Non –Current liabilities are those liabilities are those liabilities which are to be paid after a period of more than a year from the end of the accounting period.

Example-Long-term loans, debentures

Note: Contingent Liability (Doubtful liability)

These are not real liabilities. **Future events can only decide** whether it is really a liability or not. Due to their uncertainty they are termed as contingent (doubtful) liabilities. The value of contingent liabilities never shown in the amount column at the liability side of Balance sheet. It is clearly state as a note inside/outside the Balance Sheet.

Example:

- Value of bills discounted (There is a chance to **dishonor** it)
- Cases pending in the court (Court's decision may be favorable or unfavorable)
- Guarantees undertaken by the business

Capital

Amount invested by the owner into the business is known as capital. Capital contribution may be in the form of cash or assets. Capital is an obligation to the business and it is the owner's claim on the assets of the business. Capital is also known as owner's equity.

Capital= Assets- Liabilities

Drawings

Any cash or goods withdrawn by the owner for his personal use from the business or any private payments made out of business funds are called drawings. Drawings will reduce the owner's capital.

Example:

- Amount withdrawn by the owner for his personal use
- Goods taken by the proprietor for his personal use
- Acquiring personal assets with business funds.
- Owner's income tax paid by the business.

Sales

Sales means transfer of ownership of goods or services to customers for a price. It is the total revenue from goods or services sold or provided to customers. Sales may be cash sales or credit sales. It is the major source of revenue of any business.

The term 'sales' is used only for the sale of those goods which are purchased for resale purposes. (The term 'sales' is never used for the sale of assets).

Example: Sold goods to Biju for Rs.8,000, Cash sales Rs.5,000

Sales Return

Sales return or return inwards is that part of sales of goods which is actually returned to us by customers. The return may be due to defective supply of goods, violation of terms of agreement etc.It should be deducted from sales to calculate Net Sales.

Example: Goods returned by Biju Rs.400

Purchases

Purchases are total amount of goods procured by a business on credit and on cash for use or sale. The term purchase is used only for the purchase of 'Goods'. It is the major expense of a business concern.

In case of manufacturing concern goods means purchase of raw materials for the purpose of conversion of finished products and then sale. In case of trading concern 'goods' are those things which are purchased for resale. In both the cases the purpose is to make a profit by its resale. The term purchases include both cash and credit purchases of goods.

Example:

- Purchased goods from Anju traders Rs.5000
- Purchased goods for cash Rs.4000
- A furniture merchant purchased chairs for Rs.8000 is considered as purchase because here chair is his goods and its purpose is to resale and to earn profit. But if a furniture merchant purchase chairs for his office use, it is never considered as purchase, its purpose is not resale but helps to generate imcome.Here chair is an asset.

Purchase Return

When purchased goods are returned to the suppliers, these are known as purchase return or return outwards. It should be deducted from purchase to calculate Net Purchase.

Example: Returned goods by Anju Traders Rs.300

Revenues

Revenue of a business constitutes Sales revenue and other revenues. The amount earned by business by selling its products or providing services to customers are called sales revenue. Sales are the major revenue of a business. Other items of revenue common to many businesses are: commission received, interest received, dividend received, royalties, rent received etc.
Total Revenue = Sales Revenue + Other Revenue

Expenses

Expenses are costs incurred by a business in the process of earning revenue. It is the cost of use things or services for the purpose of generating revenue.
Example:
Cost of things like Purchase cost of goods, stationery etc.
Cost of services like salary, advertisement, insurance, electricity, telephone, repairs etc.
Decline in the value of asset caused by the use of such assets for business like depreciation.

Expenditure

Expenditure is funds used by a business to attain new assets, improve existing ones, or reduce a liability. Expenditure can be classified into capital expenditure and revenue expenditure.

Capital Expenditure

Expenditure which has been incurred to derive long term advantage for the business is a capital expenditure. Capital expenditure is concerned with acquiring fixed assets, increasing the value of fixed assets or investment made to increase the earning capacity of the business. The benefit of capital expenditure must extend more than one fiscal year and they are non- recurring in nature.

Example:

Amount spent to purchase fixed assets like land and building, P& M, Furniture, Goodwill etc

Revenue expenditure

Revenue expenses are shorter-term expenses that are broken down into two categories:

Expenditures for generating revenue include expenses required to meet all day-to-day expenses needed to operate a business.

Example: Salaries, wages, rent, advertisement, depreciation etc.

Expenditures for maintenance of revenue-generating assets Revenue expenditures are often discussed in the context of fixed assets .It include expenses like ordinary repair and maintenance costs that are necessary to keep the asset in working order.

Difference between Capital and Revenue Expenditure	
Capital Expenditure	**Revenue Expenditure**
Expenditure incurred for acquiring or improving fixed assets not meant for resale.	It is a routine expenditure incurred to meet the day to day expenses and includes cost of sales and maintenance of fixed assets
Increases earning capacity	Maintains the earning capacity
Non recurring in nature	Recurring in nature
It produces benefits over several years	Its benefit will be consumed within an accounting year
It is an item of Balance Sheet	It will show in Trading and Profit & Loss A/C

Profit

Profit is the excess of revenues over expenses in an accounting year. Profit increases the investment/capital of the owner. Profit is calculated by deducting the cost from the sale or revenue, which is **earned by the regular business transaction**.

Gain

A gain is referred to as any economic benefit derived from **outside of the usual business operations**. A profit that arises from events or transactions which are incidental to business such as profit sale of fixed assets, winning a court case, appreciation in the value of an asset.

E.g. Consider an investor purchasing 1000 shares of a company at Rs. 15 each (value = Rs.15000) in 2017 and if the share price in 2018 has increased to Rs.20 each the value in 2018 is Rs. 20000, where the investor will make a **gain** of Rs. 5000 if the shares are sold in 2018.

E.g. If the book value (purchase cost- accumulated depreciation) of a machine is Rs.2,500 and it was sold for Rs.3,000 then the **gain** on disposal is Rs.500

Profit	Gain
Profit is the excess of total income over total expenses	Gain is the benefit derived from outside of the usual business operations like profit on sale of fixed assets etc
It is generated from usual business operations	It is generated outside of business operations

Income

Income is the increase in the net worth of an organization either from business activity or from other activities.

Income=Profit + Gain

Loss

Loss is excess of expenses of a period over its related revenues. It decreases in owner's equity. The term loss conveys two different meanings.

First it conveys the result of the business for period when total expenses exceeds total revenues.

Example-If revenues are 3, 00,000 and expenses are 3, 50,000, the loss will be Rs.50, 000.

Second, It refers to money or money's worth lost (or cost incurred) without receiving any benefit in return, e.g., cash or goods lost by theft or a fire accident, etc. It also includes loss on sale of fixed assets.

It may be noted that losses differ from expenses. Expenses are incurred to generate revenues whereas losses do not.

Discount

Discount is a rebate or an allowance given by the seller to the buyer. It is offered in two ways-discount offered at the time of sale (Trade discount) and discount offered at the time of collection of sales price from debtors (Cash discount)

Trade Discount-When goods are purchased in bulk quantities, the seller may give certain concession on the listed price to the buyer. This concession is called trade discount. It is not recorded in the books of account as it is deducted in the invoice (bill) itself from the gross value of goods.

Example-Purchased goods worth Rs 50,000 from Rajan at a trade discount of 10%.Here value of purchase is recorded as Rs.45,000 (50000-5000).Therefore trade discount Rs.5000 never recorded in the books of account.

Cash Discount-When discount is allowed to the customers for making prompt (timely) payment, it is called cash discount. It is always recorded in the books of account. It is a loss to the creditor (discount allowed) and a gain to the debtor (discount received)

Example-Received cash from Mohan Rs.3850 allowed him discount Rs.150 and settled his account Rs.4000.

Debtors/Account Receivables

A debtor is a person who owes money to the business for buying goods and services on credit. The total amount standing against such persons and/or entities on the closing date is shown in the balance sheet as sundry debtors on the asset side.

Example

- Sold goods to Vijayan on credit Rs.40, 000.Here Vijayan owes Rs.40,000 to the business, so he is a debtor.

Creditors/Accounts Payable

Creditor is a person/or other entities to whom the business owes money as he has given some benefit to the business. The total amount standing to the favour of such persons and/or entities on the closing date is shown in the Balance Sheet as sundry creditors on the liabilities side.

- Purchased goods from Meera Traders on credit Rs. 3000.Here business owes Rs.30000 to Meera traders, so Meera Traders is a creditor to the business.

Goods

Goods include all those things which are purchased for resale or raw materials which are used for producing the finished products.

Example:

Kalyan Silks purchased 100 shirts for Rs.12500 from Aravind Mills Ltd.Here,shirt is the goods for Kalyan Silks.

Note:

- For a furniture dealer purchase of chairs and tables is termed as goods, while for others business firm it is furniture and is termed as an asset.
- For a stationery trader, stationery is goods, whereas for others it is expense.

Drawings

Withdrawal of money or goods by the owner from the business for personal use is known as drawings. Drawings reduce the investment (Capital) of the owners.

Example

- Rajan, proprietor withdraws Rs.5000 for personal purpose.
- Owner withdraws goods worth Rs.200 for personal purpose.

Stock

The goods lying with a business for sale on any given date are called stock. The value of goods remaining unsold at the end of an accounting period is known as closing stock.

Closing stock in case of manufacturing concern consists of raw-materials; work –in – progress and finished goods. The closing stock of a particular year becomes the opening stock for the next year.

Voucher

Voucher is a documentary evidence of a business transaction. For example, if we buy goods for cash, we get cash memo, if we buy on credit, we get an invoice; when we make a payment, we get a receipt and so on.

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Luca Pacioli-Father of Accounting

In 1494, the first book on double-entry accounting was published by Luca Pacioli.He is considered as '**Father of Accounting and Bookkeeping**'. He was an Italian Mathematician.

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