

CHAPTER-1 - Meaning and Objectives of Accounting

Question 1

The method of interpreting, reporting, recording and summarizing of financial data is known as Accounting. Accounting introduction provides data about the economic condition of the business, which helps the top management of a company to make sound decisions. In today's world, to be well versed in accounting is considered a valuable knowledge as it is used by everyone. Accountancy plays the role of the "financial language".

Question 2

Those individuals / institutions are termed debtors who purchased items that are sold or service from the company on credit and the amount is due from them, whereas, those individuals / institutions are called creditors from whom the company purchased items or services on credit and the amount is due to them.

Question 3

Cash discount is the discount given to customers who make prompt payments. Cash discounts have to be noted down in the account books.

Question 4

Debtors are the individuals / institutions who purchased goods sold or service from the company on credit and the amount is due from them, whereas, creditors are the individuals / institutions who the company purchased goods sold or service from them on credit and the amount is due to them.

Question 5

Profit or loss of a specific period of time is ascertained by making the trading, profit and loss accounts.

Question 6

By creating and tallying a balance sheet, the final position of a company can be established.

Question 7

The division of commerce, that keeps a record of the financial transactions (activities) in a set of books is called book keeping.

Question 8

The objective of book-keeping is to maintain a record of transaction of a business in a systematic manner, on the other hand, accounting ascertains the profit or loss and the financial position of a company.

Question 9

The financial statement (profit and loss account and balance sheet) are the end products of financial accounting as well as reports and documents that provide information to the stakeholders about the profitability and financial position of a company.

Question 10

Owners of the company and creditors are two users of accounting information.

Question 11

The individuals who are involved in management and operation related information of the company like the owners/ partners,

directors, managers, officers, etc. are the internal users of accounting information.

Question 12

Potential investors, creditors, labour unions, customers, government, etc. are the external users of accounting information.

Question 13

Information about risk and return on investment in the company is the nature of information required by investors.

Question 14

The credit worthiness and the ability of the enterprise to pay interest as well as the repayment of the loans is the type of information required by long-term investors.

Question 15

Continuous information regarding costs, sales, profitability, etc. is the information needed by the management which are used for planning, controlling, and decision making.

Question 16

Mention two advantages of accounting.

Answer: Two advantages of accounting are:

- (i) It gives a complete, chronological and systematic record of financial transactions
- (ii) It ascertains the profit or loss of the company.

Question 17

The accounting process is done based on the historical cost, i.e. the value at the time when the transaction took place, and hence does

not account for any change in the market price which proves to be a limitation.

Question 18

Comparability and reliability are two qualitative characteristics of accounting information.

Question 19

Comparability is the qualitative characteristic of accounting that requires the use of a common unit and format of reporting.

Question 20

Reliability is the qualitative characteristic of accounting information that require it to be verifiable and free from personal bias.

Question 21

(i) To give a complete, chronological and systematic record of financial transactions

(ii) To ascertain the profit or loss of the company.

Question 22

Recording of financial transactions is the traditional function of accounting.

Question 23

A few characteristics of Accounting are.

- **Financial Transactions-** Transactions or items related to the financial character are the only transactions to be recorded in accounting.
- **Economic Value-** Any transaction not involving money is not recorded in accounting

- **Classifying-** After recording financial transactions in a journal or any subsidiary book, classification of these transactions is the next step. Classification refers to the segregation of transactions into separate accounts. The Ledger book is used to record each type of transaction according to its nature.
- **Summarizing-** The process by which all the accounts in the Ledger book are presented to the management and other users in an understandable and useful manner.
- **Interpretation -** Accounting gives complete and detailed information about the company's profits and the financial status of a company to various stakeholders, including the bank, employees, investors, creditors, etc.
- **Communicating-** Accounting involves communicating the interpreted results at the correct time and to the right stakeholders to ensure timely and efficient decisions are made.
- **An art as well as a science-** As an art, accounting has a technique to achieve pre-determined objectives. Recording, classifying, and summarizing all the financial transactions of a company is the technique, and to determine the net profit and financial position of the company is the objective. It is also a science because it is an organized body that is based on established accounting standards and particular principles.

Higher-Order Thinking Skills (HOTS) Questions

Question 1

Recording of financial transactions is the traditional function of accounting.

Question 2

To maintain a systematic records of financial transactions is the basic objective of book-keeping.

Question 3

No, I disagree. Accounting also provides relevant information to the management and the communication of financial information to the stakeholders are also the objectives of accounting apart from recording of financial transactions and preparing financial statements

Question 4

The recording of transactions in the books of accounts is the first step of the accounting process.

Question 5

Communicating the final results to the stakeholders of the company who analyse them as per their individual requirement is the final step of the accounting process.

Question 6

The appointment of Mr. Vadera will not be recorded in the accounting books of the firm because it has not resulted in any

change in the financial position of the firm. The payment of ₹50,000 per month as salary to Mr. Vadera when payed will be recorded in the accounting books.

Question 7

The decision is not justified because the comparability of current year figures with that of the previous year is a qualitative characteristic of financial information. Cease of this practice will result in the termination of a valuable practice being followed by the company.

Question 8

Two examples of transactions that are not recorded in accounting are:

- (i) Resignation by the Vice President
- (ii) Appointment of new Sales Manager

Question 9

No, this will not be recorded in the books as it is only the receipt of an order and has not resulted in any exchange of goods/ services nor a change in the financial position of the firm.

Value-Based Questions

Question 1

A comparison of current performance with past performance is enabled by giving the figures for the previous year along with the figures of the current year.

Question 2

No, this will not be recorded in the books of account of the business as the property belonged to Mr. Ganpati and is not a property of the business. If Mr. Ganpati decides to invests this amount in the business it will be recorded in the books of the business and will be treated as additional capital introduced by the proprietor.

Question 3

Explanatory notes help make the financial statements more useful and understandable.

Question 4

The appointment of Ms. Arun will not be recorded in the accounting books of the school because it has not resulted in any change in the financial position of the school. The payment of ₹30,000 per month as salary to Ms. Arun when payed will be recorded in the accounting books.

Question 5

Comparability of assets is possible in adopting the same method of depreciation year after-after.

Question 6

Yes, it will be recorded in the books of account and will be treated as drawings in the form of goods by Miss. Priti.

Question 7

The accountant has to utilize his sense of judgment in regard to various transactions. For instance, it is difficult to forecast with absolute accuracy the actual functioning life of an asset which is required for calculating depreciation on it. The same is applicable

about making provision for doubtful debts and the method used for the valuation of stock.

Question 8

As per accounting standard 26 (Intangible assets), self-generated goodwill is not recorded in the books of accounts because consideration in money or money's worth has not been paid for it. Hence the goodwill considered by Mr, Vishwanath will not be recorded in the books of accounts.

Question 9

The accounting process is done based on the historical cost, i.e. the value at the time when the transaction took place, and hence does not account for any change in the market price. Therefore, Mr. Yuvraj cannot change the value in the books.

Question 10

Those aspects which cannot be expressed in economic terms, such as shift in managerial roles, the goodwill of the business, employer-labour relations, firm's creative ability, management's efficiency, customer's satisfaction, etc. are known as qualitative information.

Question 11

The practice of manipulating accounts so that the financial statements may appear to be in a more favorable position than the reality is known as Window Dressing. For instance, over valuing of closing stock or not recording the purchases made at the end of the year is regarded as window dressing.

Question 12

No, the strike will not be recorded in the books of account as only transactions and events which have a monetary value can be recorded in the accounting process.

Question 13

The understanding ability characteristic of the accounting information is violated If the accounting information is not clearly presented.

Question 14

The reliability characteristic of accounting information is depicted by the trust put in that the reported information.

Question 15

The violation of values in case of window dressing are:

- (i) **Honesty** – A sense of honesty of the management towards the various stakeholders is lost, as they are not showing the true results of operations and financial position of the enterprises
- (ii) **Transparency** – Transparency of financial transactions to stakeholders is misplaced.

Question 16

Honesty and transparency are characteristics of a good accountant. All transactions must be recorded in the books of account and all facts should be disclosed. He must be disciplined and not give into pressure to hide material facts to evade tax or any other malpractices.

Question 17

The value of honesty and trust have been violated by the accountant.

Question 18

There are several events that play a role and effect the profitability of the firm, but have no economic value, and are hence ignored in the accounting process. Hence, yes, it is a limitation.

