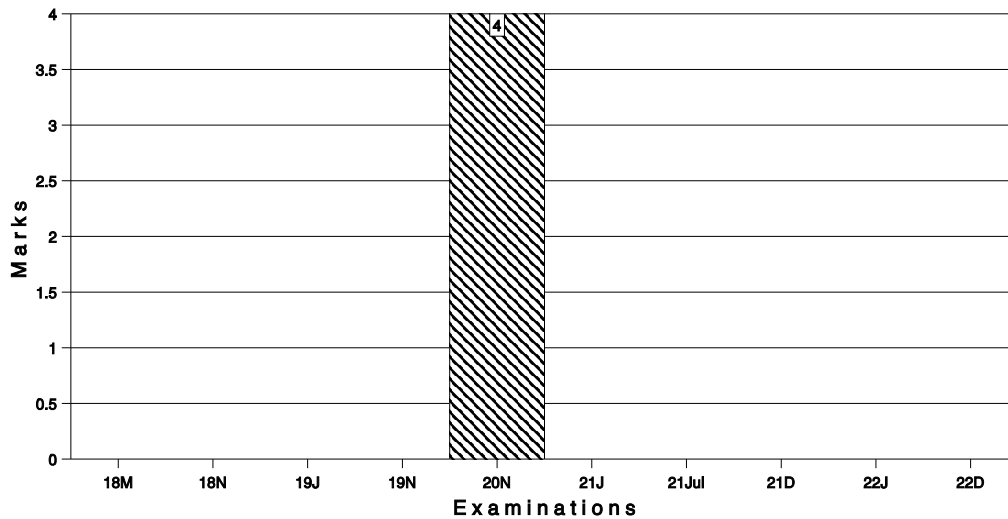
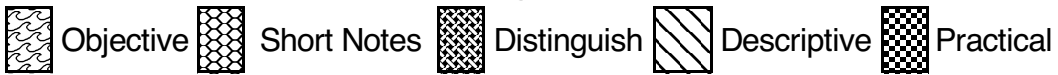


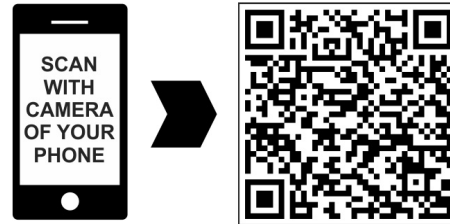
CHAPTER	<h1>Theoretical Framework</h1>
<h1>1</h1>	
Unit: 1	Meaning and Scope of Accounting

Marks of Objective, Short Notes, Distinguish Between, Descriptive & Practical Questions

Legend



For detailed analysis Login at www.scanneradda.com
for registration and password see first page of this book.



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SELF STUDY QUESTIONS

Q 1. Write Introduction to Accounting.

Answer:

In all activities (whether profit making or non-profit making) and in all organisations (like manufacturing entities, trading entities, or non-profit organisations like schools, hospitals, clubs, temples, political parties) some or the other kind of economic activities are performed. Such activities require money and other economic resources for which accounting is required to account for these resources.

Such economic activities are performed through “transactions and events”. In other words, wherever money is involved, accounting is required to account for it. **Accounting is thereby often called language of business.** Basic function of any language is to serve as a means of communication, and accounting serves that purpose.

Transactions and Events

Transaction is defined as a business, performance of an act, an agreement, while event is used to mean a happening, as a consequence of transaction, or a result. Events are the end results or conclusions of all the transactions taking place round the year.

Nalin starts a music shop by introducing capital of ₹ 5,00,000. He purchases goods worth ₹ 2,20,000, pays shop rent and electricity charges, ₹ 15,000. He sells goods worth ₹ 1,80,000 for ₹ 2,35,000.

The individual performs an economic activity. He carries on a few transactions and encounters with some events. Obviously he would want to know the result of his activities.

Result of the above activity may be ascertained as follows:

	₹
Sales	2,35,000
Less: Cost of goods sold	<u>1,80,000</u>
Gross Profit	55,000
Less: Expenses paid	<u>15,000</u>
Net Profit/Surplus	<u>40,000</u>

Earning surplus of ₹ 40,000 is an event, and closing inventory in hand ₹40,000 (2,20,000 – 1,80,000) is also an event. Introduction of capital, purchase of goods, sale of goods and payment of expenses are all transactions.

Likewise, Government collects taxes, pays salary to employees and spends on other developmental activities.

Everybody wants to keep record of all such transactions and accounting helps us to keep record of all such transactions and events.

The aim of accounting is to meet the informational needs of the rational and sound decision-makers, and thus, it is called language of business.

Q 2. Write Meaning and Definition of Accounting.

Answer:

Accounting is a process of recording financial transactions, summarising them and communicating the financial information to users viz, the proprietor, creditors, investors, government agencies, etc. It is because of these characteristics, that accounting is called the language of business.

The committee on Terminology formed by American Institute of Certified Public Accountants gave the following definition of Accounting –

“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.”

The American Accounting Association defined accounting as –
“The process of identifying, measuring and communicating economic information to permit informed judgements and decisions by the users of accounts”.

Accounting helps to ascertain the impact of events and transactions occurred during the period in terms of money. It not only helps in recording the transactions but also relates to interpreting the results thereof.

Q3. What are the Procedural Aspects of Accounting?

Answer:

(i) **Generating financial information:**

Recoding the business events and transactions of financial nature in Primary Books (Journal) and other subsidiary books with the help of invoices, sales bills, passbooks, etc.

Classification of transaction and events is done to group identical transactions together and to describe them by the name of account. This classification is done in secondary books called ledger, by posting transactions from Journal.

Summarising the transactions is the systematic presentation of recorded data so that it is understandable and useful for its users. It is the combined effect of all recorded transactions and is obtained by preparing various financial statements such as:

1. Trial Balance
2. Profit & Loss A/c
3. Balance Sheet
4. Cash flow statement.

Analysing provides the basis for interpreting the recorded data. It involves critical examination of accounting data. It is the process to evaluate the relationship between various components of financial statements.

Interpreting is the process of giving meaning to the analysed data so that proper judgement regarding profitability and financial position of business operations can be made. It helps in planning the future business activities.

Communication is the process of transmitting the financial statements in the form of accounting reports, balance sheets etc. to the users to help them in the decision making process.

(ii) **Using the Financial Information:**

Financial information is used not only by the management of business but also by other stakeholders, such as creditors, investors, employees, bankers, competitors, government etc. Various stakeholders require information related to the business for different purposes.

The financial information required for different purposes must be presented in different forms so that it meets the objective of the users which may be internal or external. Information regarding internal working should be in detail for the use by management; however, information can be in charts and graphs with less details for external users, who only want an overview of the business.

Q 4. How was Evolution of Accounting as a Social Science done?

Answer:

Phase I: The root of financial accounting system was Stewardship Accounting. This traditional approach of accounting places an obligation on stewards or agents to manage the property and provide relevant financial information relating to their resources to the owner which were usually the wealthy persons or businessmen.

Phase II: Then emerged the idea of joint stock company in the second phase of evolution. It is a type of business organisation with the basic idea of separating ownership from the management. For better disclosure of financial data, various tools such as profit and loss account and Balance Sheet were introduced.

These were the information systems used by the different users such as investors, employees, managers, and other stakeholders for getting meaningful information.

Phase III: Then came the new dimension of accounting in the third phase called as Management Accounting, which was seen as “value creator”. It was developed in 20th century. Its focus was to apply professional knowledge and skills in such a way so as to assist the management in making quality

decisions.

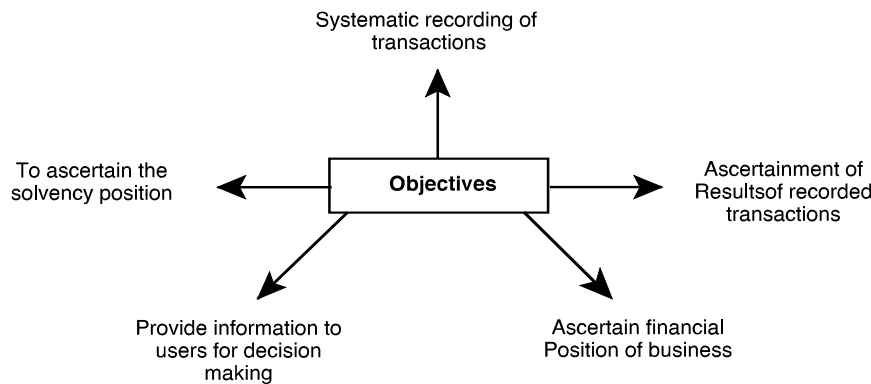
Phase IV: Social Responsibility Accounting is the process of communicating the social and environmental effects of an organisation's actions to particular groups of society and society at large. It broadens the scope of accounting in a sense that it should:

- concern itself with more than only economic events;
- not be exclusively expressed in financial terms; and
- be accountable to a broader group of stakeholders beyond reporting financial success.

Social Science studies man as a member of society and concerns about social purposes, contribution to the social progress. Hence, Accounting is treated as **social science**.

Q 5. What are Objectives of Accounting?

Answer:



1. **Systematic recording of transactions** – of financial nature for further analysis. Recording is usually done in Journal or other subsidiary books and the entries are later posted to secondary books (ledger) on the basis of classification.

2. **Ascertainment of Results of recorded transactions** – by keeping proper records of expenses and revenue.
If income/revenue < expenses = Loss.
If income/revenue > expenses = Profit
This is calculated by preparing Profit and loss Account. It helps management to take necessary actions accordingly.
3. **Ascertainment of financial position of business** – by preparing a Balance Sheet. A Balance Sheet is a statement of Assets and liabilities of the business organisation which serves as a barometer for ascertaining the financial health of business at a particular point of time or date.
4. **Providing information to users for rational decision making** – who analyse it as per their individual needs at the required point of time. Information is provided by preparing and communicating financial statements to various stakeholders for the purpose of decision making.
5. **To ascertain the solvency position** – If the organisation is able to meet its liabilities as and when due, in the long run, the enterprise is said to be solvent. Also, organisation must maintain its liquidity position so as to meet its short-term liabilities at relevant due date.

Q 6. What are Functions of Accounting?

Answer:

- (i) **Measurement:** Accounting helps the business organisation to measure its financial performance of earlier years along with current position.
- (ii) **Comparison:** It facilitates comparison of financial position of earlier years with the current year.
- (iii) **Evaluation:** Accounting helps to evaluate the financial results of a business organisation by providing proper disclosures about the accounting policies used in preparation of books of accounts.
- (iv) **Forecasting:** 'It helps in predicting the future business activities by using the past data.
- (v) **Control:** Accounting keeps a check on operational system and thus identifies weaknesses which can be overcome by implementing necessary measures.

- (vi) **Government Regulation and Taxation:** Accounting information helps the government to keep a check on business activities and facilitates collection of various taxes.

Q 7. Define Book Keeping.

Answer:

1. Book keeping is the systematic recording of financial transactions on a day to day basis.
2. It includes –
 - Recording of transactions and events in books of Accounts.
 - Classifying the recorded transactions and events in ledger [i.e. posting]
3. The end product of book keeping is the 'financial statements' which includes Profit and Loss A/c, Balance sheet, Notes to Accounts and Cash flow statement.
4. The transactions of financial nature [which are related to money] are recorded. For, example Appointment of a director or employee in the company is not a financial transaction, hence need not be a part of book keeping. On the other hand if a loan is given to director of ₹ 1,00,000, it is a financial transaction, and hence will be recorded as a part of book keeping.
5. The person responsible for maintaining the records of business is known as **book keeper**.
6. Book Keeping helps to know the true picture of company's income, expenses, assets, liabilities, etc.
7. Various laws such as Companies Act, Income tax Act, Banking Regulation Act, Insurance Act, etc. guide about proper preparation, presentation and preservation of books of Accounts of the company.

Q 8. What are Objectives of Book Keeping?

Answer:

1. **Complete recording of transactions** in orderly and systematic manner, so that proper documentary base is created which can be referred by any person and he is able to interpret the same.

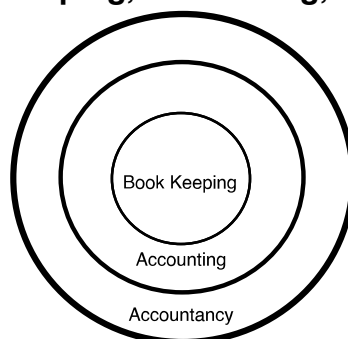
2. **Ascertain the financial effect** of the business transaction done during a specified period on the business as a whole in terms of profit or loss.
3. **To know the financial position** of business as and when required.
4. **Facilitating management** to discharge their duties by providing information for taking business decisions.

Q 9. Differentiate between Book Keeping and Accounting.

Answer:

Basis of Difference	Book Keeping	Accounting
1. Scope	Recording of transaction in a systematic manner	Summarising of the recorded transactions
2. Stage	Primary Stage or initial stage	Accounting begins where book keeping ends.
3. Decision-making	Cannot be done	Can be done.
4. Nature of job	Clerical and routine. Can be done by lower staff	Analytical in nature and requires special knowledge and ability.
5. Objective	Accurate and complete record of financial transaction of business.	Apply further financial analysis to financial records.
6. Financial Position of business	Cannot be ascertained	Can be ascertained.

Relationship of Book Keeping, Accounting, and Accountancy.



Book Keeping is the primary function of accounting and focuses on proper recording and maintenance of books of accounts.

Accounting is the secondary function. It **starts where book keeping ends**.

Accountancy is the systematic knowledge applied in the process of accounting.

It can be said that accountancy is a broader term that acts as a guide for preparation of books of accounts and it involves book keeping and accounting.

Q 10. What are the Sub Fields of Accounting?

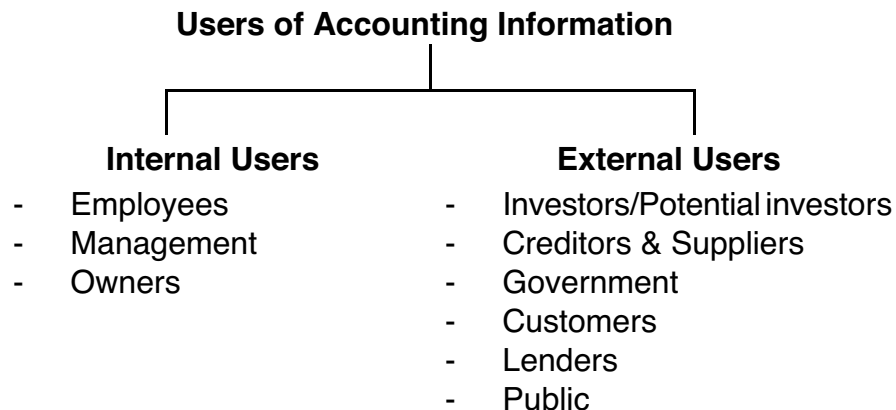
Answer:

- 1. Financial Accounting:** It is concerned with recording, summarising and interpreting the financial transactions and communication of the same to the users.
It focuses on preparation of profit and loss account and balance sheet to ascertain the financial position of business at the end of an accounting period.
- 2. Management Accounting:** It is a recent development in accounting. It deals with the aspect of costing and cost control. It includes costing department which keeps records of various products and services. It is the process of analysis, interpretation and presentation of accounting information collected with the help of financial accounting and cost accounting in order to assist the managerial staff in decision making and day to day operations of the business.
- 3. Cost Accounting:** It ascertains the cost of products manufactured or the services rendered and helps the management in taking pricing decisions and exercising control. According to Institute of cost management accounts of England, "Cost Accounting is the process of accounting for cost which begins with the recording of income and expenditure or the base on which they are calculated, and ends with the preparation of periodical statements and reports for ascertaining and controlling costs.

4. **Social Responsibility Accounting:** It is the ability to provide correct information in company's financial statements regarding the estimated social cost and social benefits generated due to business operations. For example, if a factory is setup, it will benefit the society by way of generation of employment opportunities crates etc. Similarly, if a product is found defective or harmful to the users then it may adversely affect the image of the company. The organisations which creates value for its users and society usually survive in the long run. Thus, the demand of social responsibility accounting has increased.
5. **Human Resource Accounting:** It is the process of assigning, budgeting and reporting the cost of human resources incurred by an organisation. It includes salaries or wages paid, training expenses, recruitment costs, etc. It is a new branch of accounting which includes the management of human resource which will ultimately enhance the quantity and quality of goods and services.

Q 11. Who are the Users of Accounting Information?

Answer:



Internal Users:

(a) Employees

- They have direct relationship with the growth of the business organisation.
- They are entitled to incentives linked to profit earned by the business and thus are interested in financial statements.

(b) Management

- Accounting information acts as a guiding tool for various managerial decisions such as ascertaining the selling price of a product, investment in a new project, market entry strategy, etc.
- They are concerned with using their expertise knowledge about the business operations to improve the performance and increase the efficiency within the company.

(c) Owners

- They are the persons who contribute towards the capital of the business and are therefore exposed to business risk.
- Owners are concerned with the profits and losses of the business.

External Users:**(a) investors or Potential investors**

- Accounting information helps the investors to know the return on investment made, or to be made.
- It helps them to know how safe is their investment and also whether the business will survive, prosper and pay good dividends, or not.

(b) Creditors & Suppliers

- Creditors are those who supply goods and services to the business organisation and are concerned whether business will survive in a long run.
- Before granting credit, creditors want to satisfy themselves about the credit worthiness of the business and formulate credit policy accordingly.

(c) Government

- Government regulates day to day activities of the business, and imposes various taxes. Therefore, it is necessary for it to inquire into the financial statements of the business organisation to find whether the correct account of taxes due are paid, or not.
- Accounting information also helps the government in price fixation of essential commodities, compilation of National Income and other necessary information.

(d) Customers

- Customers are concerned with the fact whether the company offers products at fair prices, and its survival, for honouring product warranties.
- They want to know about the stability and profitability of the business enterprise since they are dependent on products and services of such businesses.

(e) Lenders

- They are the providers of loan funds and hence want to assure themselves about the recovery of loans alongwith interest, if any, as and when due.
- “Lenders” includes banks & financial institutions which are interested to know the performance of business, whether the business is flourishing as projected at the time of raising of loan, or do the terms of loans need to be revised.

(f) Public

- Public needs to know whether the business is contributing substantially for the growth of economy, or not.
- Public also wants to know whether the products and services provided are useful, for providing employment to the public without adversely affecting the environment.

Q 12. What is the Relationship of Accounting with other disciplines?

Answer:

1. Accounting and Economics:

- Economic theories help to develop the decision making tools which are used in accounting. Accountants gets the idea about income, value, capital maintenance, etc. from economics and applies the same in accounting of business operations.
- Economics is regarded as science of rational decision making for use of scarce resources efficiently to satisfy the human wants. Accounting provides financial data which is relevant for taking such decisions.

- Accountants use various methods to analyse expenses, incomes, budgets etc., whereas economics on the other hand is concerned with interpreting the financial patterns for understanding the economic behaviour of such transactions, and takes rational decisions for the business.

2. Accounting and Statistics:

- Statistics deals with typical values, behaviour, trends of a given period of time and the degree of deviation over a series of observations while accounting focuses on accuracy in recording of financial transactions of business.
- The main object of both is to make arithmetical figures in such form which is understandable and usable to the management and other concerned parties.
- Various accounting and financial ratios are formulated on the basis of statistical method. Accounting records are usually viewed for short term, however statistical analysis takes long term view of events.

3. Accounting and Mathematics

- For accounting, it is necessary to have to knowledge of algebra, arithmetic for calculation of interest, lease rentals, depreciation, tax due, penalties, etc.
- For better understanding of financial information, analysts use various presentation tools such as matrix, graphs, charts, and hence it has become essential to have knowledge of geometry, trigonometry for proper understanding.
- Accounting expression can be expressed in algebraic forms. For example double entry book keeping can be stated in algebraic form
$$\text{Assets} = \text{Liabilities} + \text{Equity}.$$

4. Accounting and Law

- All the transactions of a business organisation are governed by several Acts such as contract Act, companies Act, sales of goods Act, Labour Laws, etc. These laws need to be followed to prevent the organisation from being penalised due to non-compliance.

- There cannot be enactment of legislation about accounting system unless accounting discipline is developed correspondingly. Therefore, it can be said that accounting influences law and is also influenced by laws.

5. Accounting and Management

- Management decisions are based on accounting data provided by the accountant. Accountants are thus required to present the data in an understandable and usable manner.
- With the information provided by accountants, management is able to analyse past performance of business organisation, and accordingly plan future operations.
- Various functions of management are linked with accounting. For example – Planning of budget requires costing of a product; controlling function requires management to control cost/expenditure which can only be done if management is aware about the standard cost to be incurred for a product and the excess or deficit in actual cost in making of the product. All this requires accounting data. Hence, we can say that both the disciplines are related to each other.

Q 13. What are Limitations of Accounting?

Answer:

- Various qualitative factors are ignored such as expertise and knowledge of managerial personnels, loyalty of employees, etc., although responsible for success of business, as they are not measurable in term of money.
- Accounting for future projections are done on basis of various assumptions and estimations which may not hold good if conditions change in future in an unpredictable manner.
- Accounting ignores time value of money for recording transactions.
- Selection of different methods for calculation of depreciation such as SLM, WDV, method of calculation of valuation of closing stock such as LIFO, FIFO etc. may give different results for the financial period.
- Selection of methods, assumptions, etc., may vary from organisation to organisation. Hence, it becomes difficult to compare the two organisations.

- Financial statements are subject to window dressing, and hence, may not show the true picture of the business operations and financial position of the company.
- Accounting is based on personal judgement of accountants for various estimates, and hence, may provide different results from time to time.

Q 14. What is the Role of Accountant in the society?

Answer:

Accounting profession serves the society in various ways such as —

A. Areas of Services

1. **Maintenance of Books of Accounts** of business and preparation of financial statements such as profit and loss account, Balance Sheet, which assist various users for decision making.
2. **Taxation:** Accounting records helps to assess the tax liability of a person and also assists in tax planning.
3. **Analysis:** Accounting Data of various years is compared, and thus, the performance of business can be monitored.
4. **Statutory Audits:** Books of Accounts must give true and fair view. For limited companies, statutory audit is necessary, which must be done by a Chartered Account or a firm of Chartered Accountants.
5. **Internal Audits:** To ensure that proper controls are implemented by the management over the assets of company and preparation of financial statements, firms appoint internal Auditors who are responsible to check controls and communicate deficiencies, if any, to management in a timely manner.
6. **Management and Consultancy Services:** Various functions of management, including decision making, requires financial data. Hence, Accountant may play advisory role in such decision making process.
7. **Financial Advice:** Accountants are believed to be financial literate persons, i.e., having expertise knowledge, and so they can give advice in areas such as—
 - (a) Insurance
 - (b) Business Expansion

- (c) Investment
- (d) Sale of business
- (e) Tax relief under various Pension Schemes

8. Investigation: Accountants are required to investigate into various financial matters such as:

- (a) Variation in profit figures as compared to previous years.
- (b) Costing of a product or service rendered.
- (c) Detection of Fraud and remedial action required to lower the impact of such fraud.
- (d) Valuation of business for ascertaining correct tax liability, for purchase or sale of business, etc.

9. Other Services:

- (a) Portfolio Management
- (b) Secretarial Work
- (c) Company incorporation
- (d) Feasibility study
- (e) Arbitration
- (f) Share Transfer and Registration work
- (g) Act as a liquidator, Receiver, Arbitrator
- (h) Cost Accounting Work
- (i) Supply of information.

B. Chartered Accountants in Industry

- Act as financial advisor of management for planning future activities.
- Performs various business functions such as setting of budgets, ascertaining cost of product, calculation of profit linked bonus of employees, etc.

C. Chartered Accountants in Public Sector

- Preparation of report of public corporations to know whether the expenditure by several departments exceeds the budget sanctioned to them, or not.
- To keep a check, whether the Public Sector units are performing their functions properly, challenges faced by them, if any, and making the general public aware about the authenticity of various items appearing in financial statements and other reports.

D. Chartered Accountant in Framing Fiscal Policies

- Fiscal Policy is the spending made by the government which influences the economy of the nation. Accountants help in development of trade, commerce, industry, and hence, help to determine suitable fiscal policies.
- There is a social responsibility on Accountants along with the industry to give true and correct disclosures regarding financial results as are necessary in calculation of national income.

E. Chartered Accountants and Economic Growth

- High quality corporate reporting helps in transparency and mobilisation of various investments and generating confidence among investors across the globe, hence facilitating economic growth of the nation.
- Chartered Accountants are responsible for proper reporting and encouraging the business organisations for efficient working and true and fair disclosures. This, in turn, contributes to the growth of the economy.

**Questions for Practice and Conceptual Clarity only
(The questions below have been given for building the
basics and increasing knowledge of the students)**

MULTIPLE CHOICE QUESTIONS

1. The main objectives of Book-Keeping are:
 - (a) Complete Recording of Transactions
 - (b) Ascertainment of Financial Effect on the Business
 - (c) Analysis and Interpretation of data
 - (d) (a) and (b) both

2. At the end of the financial year, after sale of goods worth ₹2,00,000, there was a closing stock of ₹10,000. This is:
 - (a) An event
 - (b) A transaction
 - (c) Both event as well as transaction
 - (d) None of these
3. Financial Statements are a part of:
 - (a) Accounting
 - (b) Book - Keeping
 - (c) Both
 - (d) None
4. _____ of American Institute of Certified Public Accountants enumerated the functions of Accounting:
 - (a) Accounting Principles Board
 - (b) Accounting Standards Board
 - (c) Accounting Concepts Board
 - (d) None of these
5. Management Accounting:
 - (a) Is a clerical work
 - (b) Is accounting for future
 - (c) Is a recording technique of the management related transactions
 - (d) Is an analysis of the past business activities
6. The direct advantage of accounting does not include:
 - (a) Preparation of financial statements
 - (b) Competitive advantage
 - (c) Ascertainment of profit or loss
 - (d) Information to interested groups
7. Double Accounting System owes its origin to:
 - (a) Lucas Pacioli
 - (b) Adam Smith
 - (c) Kohler
 - (d) Karl Marx

8. On 31st December, 2005, Ashok Ltd. purchased a machine from Mohan Ltd. for ₹1,75,000. This is: (Year end: 31st December)
- (a) A transaction
 - (b) An event
 - (c) None of these
 - (d) Both transaction as well as event
9. The problems related to price-rise are handled under:
- (a) Management Accounting
 - (b) Cost Accounting
 - (c) Financial Accounting
 - (d) Inflation Accounting
10. Financial statements users include
- (a) Shareholders
 - (b) Government
 - (c) Vendors
 - (d) All of the above
11. Which of these is not available in the Financial Statements of a Company?
- (a) Total Sales
 - (b) Total Profit & Loss
 - (c) Capital
 - (d) Cost of Production
12. ₹5000 paid as rent of office premises is an/a _____
- (a) Event
 - (b) Transaction
 - (c) Both
 - (d) None.
13. Which of the following is correct? Owner's Equity is:
- (a) $(\text{Current Asset} + \text{PPE}) + (\text{Current Liabilities} + \text{Long term Liabilities})$
 - (b) $(\text{Current Asset} + \text{PPE}) - (\text{Current Liabilities} + \text{Long term Liabilities})$
 - (c) $(\text{Current Asset} - \text{PPE}) - (\text{Current Liabilities} + \text{Long term Liabilities})$
 - (d) None of the above.

14. If owner's capital is ₹50,000 liability is ₹30,000 and fixed assets (PPE) is ₹70,000, then what is the value of current assets?
- (a) ₹10,000
 - (b) ₹40,000
 - (c) ₹80,000
 - (d) ₹1,00,000
15. Net Profit or Loss will be derived at _____ stage of accounting
- (a) Classifying
 - (b) Interpretation
 - (c) Recording
 - (d) Summarising
16. Which one of the following is not a main objective of accounting?
- (a) Systematic recording of the transaction
 - (b) Ascertainment of the profitability of the business.
 - (c) Ascertainment of the financial position of the business.
 - (d) Solving tax disputes with tax authorities
17. At the end of the financial year, Mr. X earns a profit of ₹57,000 in his business. This is
- (a) a transaction
 - (b) an event
 - (c) a transaction as well as an event
 - (d) neither a transaction nor an event
18. Which of the following is an event?
- (a) Sale of goods for ₹5,000
 - (b) Closing stock of worth ₹4,000
 - (c) Purchase of goods for ₹8,000
 - (d) Rent paid ₹2,000
19. Accounting has universal application for recording _____ and events and presenting suitable information for decision making
- (a) Entries
 - (b) Transactions
 - (c) Data
 - (d) Figures.

20. _____ was the root of financial accounting system:
- (a) Social accounting
 - (b) Stewardship accounting
 - (c) Management accounting
 - (d) Responsibility accounting
21. Interpreting Financial Statements means:
- (a) Methodical classification of the data given in the financial statements.
 - (b) Preparation and presentation of the classified data in a manner useful to the users of financial statements.
 - (c) Systematic analysis of the recorded data so as to put information in usable form.
 - (d) Explaining the meaning and significance of the relationship of analysis of accounting data.
22. The process of recording financial data along with the preparation of trial balance are covered under:-
- (a) Book Keeping
 - (b) Accounting
 - (c) Classifying
 - (d) Summarising
23. All items relating to fixed assets (PPE) are put at one place while all items relating to current assets are put at another place. Which procedural stage of the accounting is being referred?
- (a) Communicating
 - (b) Analysing
 - (c) Interpreting
 - (d) Recording
24. Government raises funds through taxes and spends on various development activities. The deficit or surplus at the end of accounting year is:
- (a) A transaction
 - (b) An event
 - (c) A transaction as well as an event
 - (d) Neither transaction nor an event.

25. "Substance of any transaction should be considered while recording them and not only the legal form." This statement holds true for?
- (a) Substance over form
 - (b) Disclosure of accounting policies
 - (c) Both (a) and (b)
 - (d) None of the three
26. Financial position of the business is ascertained on the basis of:
- (a) Records prepared under book keeping process
 - (b) Trial balance
 - (c) Accounting Reports
 - (d) None of the above
27. On March 31st, 2016, after sale of goods worth ₹45,000, businessman is left with the closing inventory of ₹20,000. This is:
- (a) an event
 - (b) a transaction
 - (c) a transaction as well as an event
 - (d) neither a transaction nor an event
28. BOD, government, lender, suppliers, customers, managers, investors, partners. From the above identify the external and internal stakeholders.
- (a) Internal: BOD, lender, suppliers, manager, partners
External: Investor, customers, government
 - (b) Internal: BOD, managers, partners
External: Investor, customer, government, lender, supplier
 - (c) Internal: BOD, lenders
External: Suppliers, managers, partners, investors, customers, government
 - (d) Internal: BOD, partners
External: Suppliers, managers, investors, lenders, customers
29. Procedure of accounting includes two main components, namely:
- (a) Generating and using financial information
 - (b) Generating and reporting financial information
 - (c) Generating and classifying financial information
 - (d) Reporting and communicating information

ANSWER

1.	(d)	2.	(a)	3.	(a)	4.	(a)	5.	(c)
6.	(b)	7.	(a)	8.	(d)	9.	(d)	10.	(d)
11.	(d)	12.	(b)	13.	(b)	14.	(a)	15.	(d)
16.	(d)	17.	(b)	18.	(b)	19.	(b)	20.	(b)
21.	(d)	22.	(a)	23.	(b)	24.	(b)	25.	(a)
26.	(c)	27.	(a)	28.	(b)	29.	(b)		

SHORT PRACTICE QUESTIONS

- State with reasons whether following statements are **True** or **False**.
 - The term book keeping and accountancy can be used interchangeably.
 - Accounting deals with quantifiable information.
 - Accounting is the language of business.
 - Accounting aims to communicate financial information to investors only.

Answer:

(i) False.	(ii) True
(iii) True	(iv) False
- Define Accounting. What are the objectives of Accounting?
- Enumerate the advantages on Accounting.
- What are the limitations of accounting?
- Differentiate between Book keeping and Accounting.
- What are the sub-fields of Accounting?
- Write short note on 'transaction' and 'events'.
- Accounting is treated as a social science. Explain.

LONG PRACTICE QUESTIONS

1. Explain in detail different categories of users of Accounting information.
[Hint: Refer Question 11]
2. The practice of Accountancy has crossed its usual domain of preparation of financial statements, interpretation of such statements and audit thereof. Enumerate various areas of service for an Accountant.
[Hint Refer Question 14]

PAST YEAR QUESTIONS AND ANSWERS

OBJECTIVE QUESTIONS

2002 - Nov [5] State with reasons whether the following statement is True or False:

- (d) Assets and Liabilities of a particular accounting period are shown in the Balance Sheet. (2 marks)

Answer:

False: A balance sheet shows the position of the assets and liabilities as on a particular date.

2003 - May [5] State with reasons whether the following statements are true or false:

- (i) Accounting can be viewed as an information system which has its input processing methods and output. (2 marks)
- (ii) The value of human resources is generally shown as assets in the Balance Sheet. (2 marks)
- (ix) $\text{Equity} + \text{LTL} - \text{CL} = \text{FA} + \text{CA}$. (2 marks)

Answer:

- (i) **True:** Accounting is a processing system whose input is financial transaction and output is financial statements communicating various information to various interested groups.
- (ii) **False:** The human recourse still cannot be defined in terms of money.
- (ix) **False:** The correct equation is as follows:–
$$\text{Equity} + \text{LTL} + \text{CL} = \text{CA} + \text{FA}.$$

2003 - Nov [5] State with reasons whether the following statement is true or false:

- (i) Accounting involves communication. (2 marks)

Answer:

True: Accounting starts only when there is a communication of business transactions to the accounting department. It also communicates the results obtained from arranging of data to interested parties like investors, creditors, employees etc.

SHORT NOTES

1999 - May [6] Write short note on the following:

- (ii) Double Entry System. (5 marks)

Answer:**Double Entry System:**

It is a system of book keeping. It was developed in England. It is a system which recognises that every transaction has a two fold effect. Under "Double Entry System" there are two approaches of recording business transactions:

- (i) Traditional Approach i.e. Book Keeping Approach.
- (ii) Modern Approach i.e. Accounting-equation Approach.

Under the traditional approach, transactions are recorded into different books of accounts i.e. Journal, Ledger, Subsidiary Book, etc.

Under the modern approach, business transactions are recorded through accounting equation i.e. $\text{Assets} = \text{Capital} + \text{Liabilities}.$

Advantages:

1. There is a complete record of every transaction because under this system all the accounts i.e. personal, real and nominal are maintained and all the aspects of debit and credit are recorded.
2. It provides all day-to-day and reliable information.
3. It easily makes available the full details of every transaction.
4. It helps in checking of unnecessary expenditures.
5. It helps in testing of ledger posting by trial balance and also the arithmetical accuracy.
6. It helps in ascertaining the financial position of the business by preparing Balance Sheet.

2004 - Nov [6] Write short note on the following:

- (v) Role of Accountants in society. (5 marks)

Answer:

Role of Accountants in society: In the present competitive scenario, accountants play a dual role. They not only look into conventional matters relating to tax, costing, management accounting, company legislation etc., but also act in matters of modern concepts like financial policies, economic principles etc.

In brief, we can put forward the role of accountants in the following points:

- (i) They maintain the books and accounts of the business in a way that they show a true & fair view of the position of the business.
- (ii) They act as an auditor both internal and external.
- (iii) They provide service as an tax consultant.
- (iv) They act as financial advisors.
- (v) They also assist in the share registration, registration of company etc.

2005 - Nov [6] Write short note on the following:

- (ii) Qualitative characteristics of Financial Statements. (3 marks)

Answer:

Qualitative Characteristics of Financial Statements: Financial statements have some qualitative characteristics so that they may provide more information to the users. These are the qualitative characteristics of financial statements:

- (1) Understandability;
 - (2) Relevance;
 - (3) Reliability;
 - (4) Comparability;
 - (5) Faithful Representation; and
 - (6) Completeness.
- (1) **Understandability:** Required quality of information should be provided so that financial statements become more understandable for users. For this reason, it is assumed that users have a reasonable knowledge of business and economic activities and they study information with reasonable diligence. Information regarding complicated matters should be included in the statement because of its relevance to the economic decision-making needs of the users and it should not be excluded merely on the ground that it may be too difficult for some users to understand.
- (2) **Relevance:** Incorporate that information in the financial statement which is relevant for decision making. Quality of relevance of the information is determined when it influences the economic decisions of users.
- (3) **Reliability:** Information must be reliable. Level of reliability of the information is high when it is free from material errors and biased decisions. Information may be relevant but so unreliable in nature or representation that its recognition may be badly misleading.
- (4) **Comparability:** Financial Statements should be prepared in such a way that users of the financial statements must be able to compare their information with other information or financial statements in order to identify trends in performance, Cash flows, and financial position.
- (5) **Faithful Representation:** Information must be represented faithfully so that its degree of reliability is high.
- (6) **Completeness:** In order to present more reliable information in the financial statements, it must be complete within the boundaries of materiality and cost. An omission of information may cause information to be false or misleading and therefore unreliable and deficient in terms of relevance.

DESCRIPTIVE QUESTIONS

1998 - Nov [5] Discuss briefly the relationship of Accounting with:

- (i) Economics. (3 marks)
- (ii) Statistics. (3 marks)
- (iii) Mathematics. (3 marks)
- (iv) Law. (3 marks)
- (v) Management. (3 marks)

Answer:

(i) Accounting & Economics:

Accounting has some economic specialty of its own. It deals with prices and not the values. It deals with the prices of property and services and not with the property and services themselves. Accounting uses price because it can serve as a quantitative representation of the physical and actual property and services. From the viewpoint of economists, there is a very close relationship between accounting and economics. Emphasis has been laid down to test the economic theories and to apply the economic principles in the concern where accounting is a rich source. Accounting is a major supplier of information to economic agents about the various aspects.

(ii) Accounting and statistics:

Statistical methods are very helpful and useful in the interpretation and development of the accounting data. While the accounting records generally take a view of events in short term and are mainly confined to a year, a statistical analysis is more useful if a long-term view is taken for the purpose. Statistical tools are very helpful in taking decisions when they are applied to accounting data.

(iii) Accounting and Mathematics:

The dual aspect concept of fundamental accounting assumption is expressed in terms of mathematical equation, which is popularly known as Accounting Equation i.e.

$$\text{Assets} = \text{Capital} + \text{Liabilities.}$$

Mathematics has a useful impact on the users of the accounts. If the mathematics of the user is strong, its accounting may also be strong because the knowledge of mathematics helps in computations and calculations. The econometric models are also being developed for the users.

(iv) Accounting and Law:

An enterprise works under various statutory laws. The transactions and accounts are also affected by various laws such as companies Act, Sales of goods Act, Negotiable Instrument Act, Customs Act, etc. The financial statements must be prepared in accordance with relevant provisions of the applicable laws.

(v) Accounting and Management:

Accounting provides necessary information to the management for discharging its functions. Since an accountant plays an active role in management, he knows the needs of the system and data. A large portion of accounting information is made for management's decision making. Thus management and accounting are related to each other.

2020 - Nov [1] {C} (b) What services can a Chartered Accountant provide to the society? (4 marks)

Answer:

Services that a Chartered Accountant can provide to the society may include the following:

- (i) Maintenance of books of accounts.
- (ii) Statutory audit.
- (iii) Internal audit.
- (iv) Taxation services.
- (v) Management Accounting and Consultancy services.
- (vi) Financial Advice.
- (vii) Investigations.
- (viii) Secretarial work.
- (ix) Company Formation.
- (x) Arbitrations
- (xi) Liquidation of Company

(xii) Share Registration work.