# BASIC ACCOUNTING

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# IMPORTANCE AND LIMITATION OF ACCOUNTING

## IMPORTANCE

Accounting plays an vital role in running a business because it helps us to track income & expenditure, insure statutory compliance, and provide investors, management, and government with quantitative financial information which can be used in making business decisions.

**FEW MORE POINTS:**

- Accounting keeps you organized
- It backs up your tax returns
- We need is to get investment or loans
- Systematic records
- Protects business protection
- Helps in forecasting
- Helps in decision making
- Compliance with statutory provision
- Ascertainment of the financial position of the business

# LIMITATIONS

One of the biggest limitations of accounting is that it cannot measure things/ events that do not have a monetary value.

If a certain factor; no matter how important, cannot be expressed in money it finds no place in accounting

**FEW MORE POINTS:**

- Accounting is not fully exact
- Accounting ignores the qualitative elements
- Accounting ignores effect of price level changes
- Accounting is unrealistic in information
- Accounting is historical in nature
- Accounting gives overall profitability


Limitations of Accounting
01
Measurability
02
No future assessment
03
Historical cost
04
Accounting policies
05
Personal bias
06
Variability
07
Errors and frauds
08
Window dressing
09
Incomplete information
10
Others

# ACCOUNTING PRINCIPLES
## {CONCEPT AND CONVENTIONS}

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES:-
(GAAP or US GAAP) are a collection of commonly- followed accounting rules and standards for financial reporting

CONCEPTS ← PRINCIPLES → CONVENTIONS / TRADITION

**CONCEPTS**

- Consistency
- Accrual
- Going concern

Also known as
FUNDAMENTAL ACCOUNTING CONCEPTS

**CONVENTIONS / TRADITION**

- Business entity concept
- Money Measurement
- Accounting Periods
- Cost Concept
- Dual Aspect Concept
- Revenue Recognition
- Matching Concept
- Objectivity Concept
- Full Disclosure Concept
- Materiality Concept
- Concept Of Conservatism

# CONCEPTS

**CONSISTENCY CONCEPT:**

This describes that accounting principles and methods should remain consistent in order to enable the management to compare the results of the two These principles should not be changed year after year.

**GOING CONCERN CONCEPT:**

This assumes that the business will continue to exist for a long period in the future There is neither the necessity nor the intention to liquidate it.

**ACCRUAL CONCEPT:**

This helps in relating the expenses to revenue for a given accounting.

## CONVENTION

**BUSINESS ENTITY CONCEPT:**

A business and its owner should be treated separately as far as their financial transactions are concerned.

**ACCOUNTING PERIOD CONCEPT:**

According to this the entire life of the concern is divided in time intervals for the measurement of profit at frequent

**MONEY MEASUREMENT CONCEPT:**

Only business transactions that can be expressed in terms of money are recorded in accounting, though records of other types of transactions may be kept separately.

# CONVENTION

**COST CONCEPT:**

The fixed assets of a business are recorded on the basis of their original cost in the first year of accounting. Subsequently, these assets are recorded minus depreciation. No rise or fall in market price is taken into account. The concept applies only to fixed assets.

**MATCHING CONCEPT:**

This principle dictates that for every entry of revenue recorded in a given accounting period, an equal expense entry has to be recorded for correctly calculating profit or loss in a given period.

**DUAL ASPECT CONCEPT:**

According to this, every transaction has two sides at least. If one account is debited, any other account must be credited. Every business transaction involves duality of effects. (i) Yielding of that benefit (ii) The giving of that

**FULL DISCLOSURE METHOD:**

According to this , accounting reports should disclose fully and fairly the information they purport to represent. The information which are of material interest to.

**MATERIALITY CONCEPT:**

The accountant should attach importance to material details and ignore insignificant.

**CONVENTION OF CONSERVATISM:**

According to this, in the books of accounts all anticipated losses should be recorded and all anticipated gains should be.

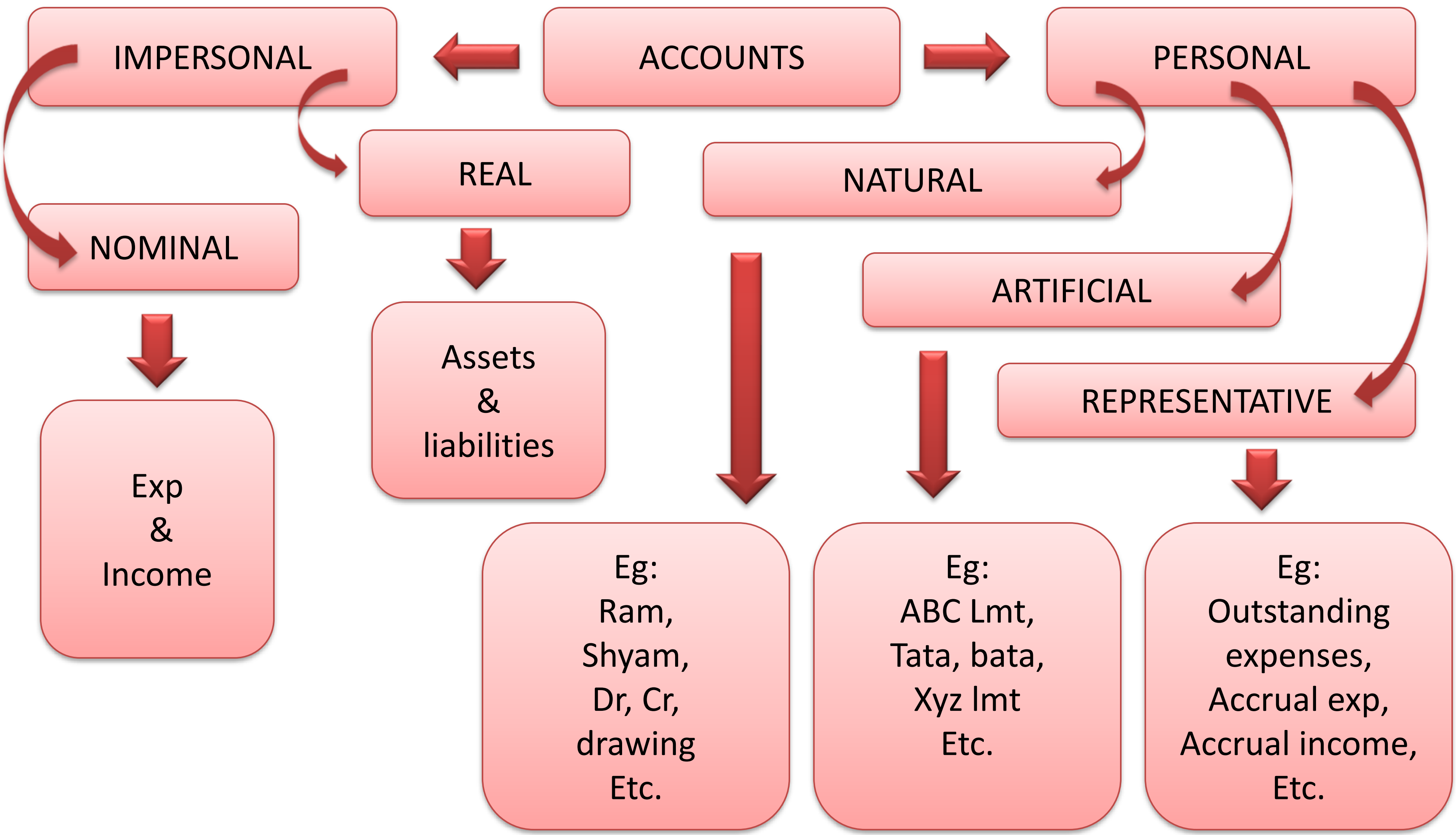
**OBJECTIVITY CONCEPT:**

This means that all accounting transactions that are recorded in the books of accounts should be evidenced and supported by business.

**REVENUE RECOGNITION:**

According to this, revenue is recognized when sale is made and sale is considered to be made when a goods passes to the buyer and he becomes legally liable to pay for.

# TYPES OF ACCOUNTS AND THEIR RULE



# EXPLAINED ABOVE MENTIONED TERMS

**PERSONAL A/C:**
A Personal account is a General ledger account connected to all persons like individuals, firms and associations. An example of a Personal Account is a Creditor Account.

**ARTIFICIAL PERSONAL ACCOUNTS:**
Personal accounts which are created artificially by law, such as corporate bodies and institutions, are called Artificial personal accounts.

**REPRESENTATIVE PERSONAL ACCOUNTS:**
Accounts which represent certain person or group directly or indirectly.

**NATURAL PERSONAL ACCOUNTS:**
Natural Persons are human beings. Therefore, we include the accounts belonging to them under this head. For instance, Debtors, Creditors, Capital A/c, Drawings A/c, etc.

# EXPLAINED ABOVE MENTIONED TERMS

**IMPERSONAL A/C:**

Accounts which are not held in the name of person are known as impersonal accounts. Any account other than personal account being classified as real account or nominal accounts is known as impersonal account.

**REAL IMPERSONAL ACCOUNTS:**

A Real Account is a general ledger account relating to Assets and Liabilities other than people accounts. These are accounts that don't close at year-end and are carried forward. An example of a Real Account is a Bank Account.

N**OMINAL IMPERSONAL ACCOUNTS:**

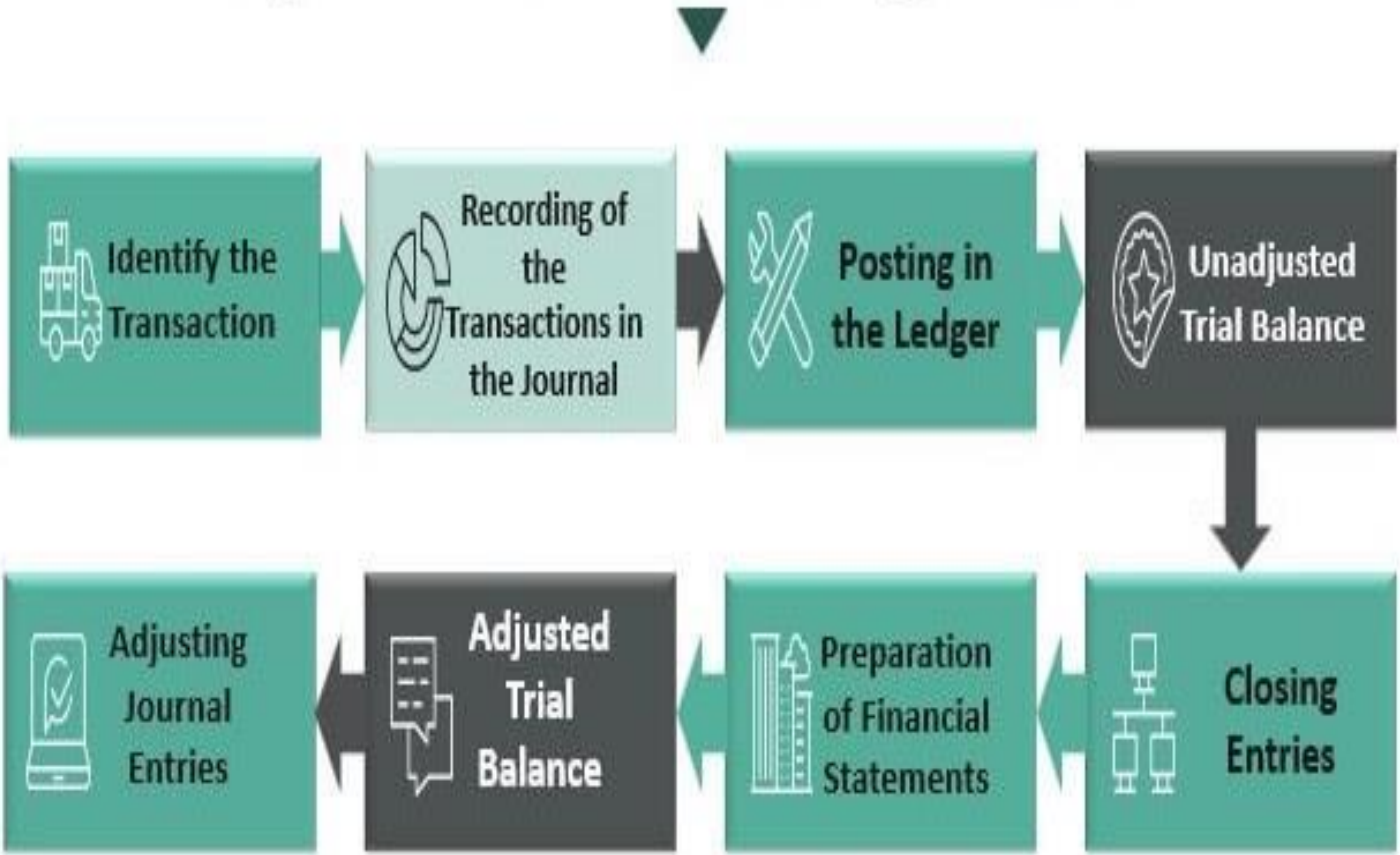
A nominal account is an account in which accounting transactions are stored for one fiscal year. At the end of the fiscal year, the balances in these accounts are transferred into permanent accounts

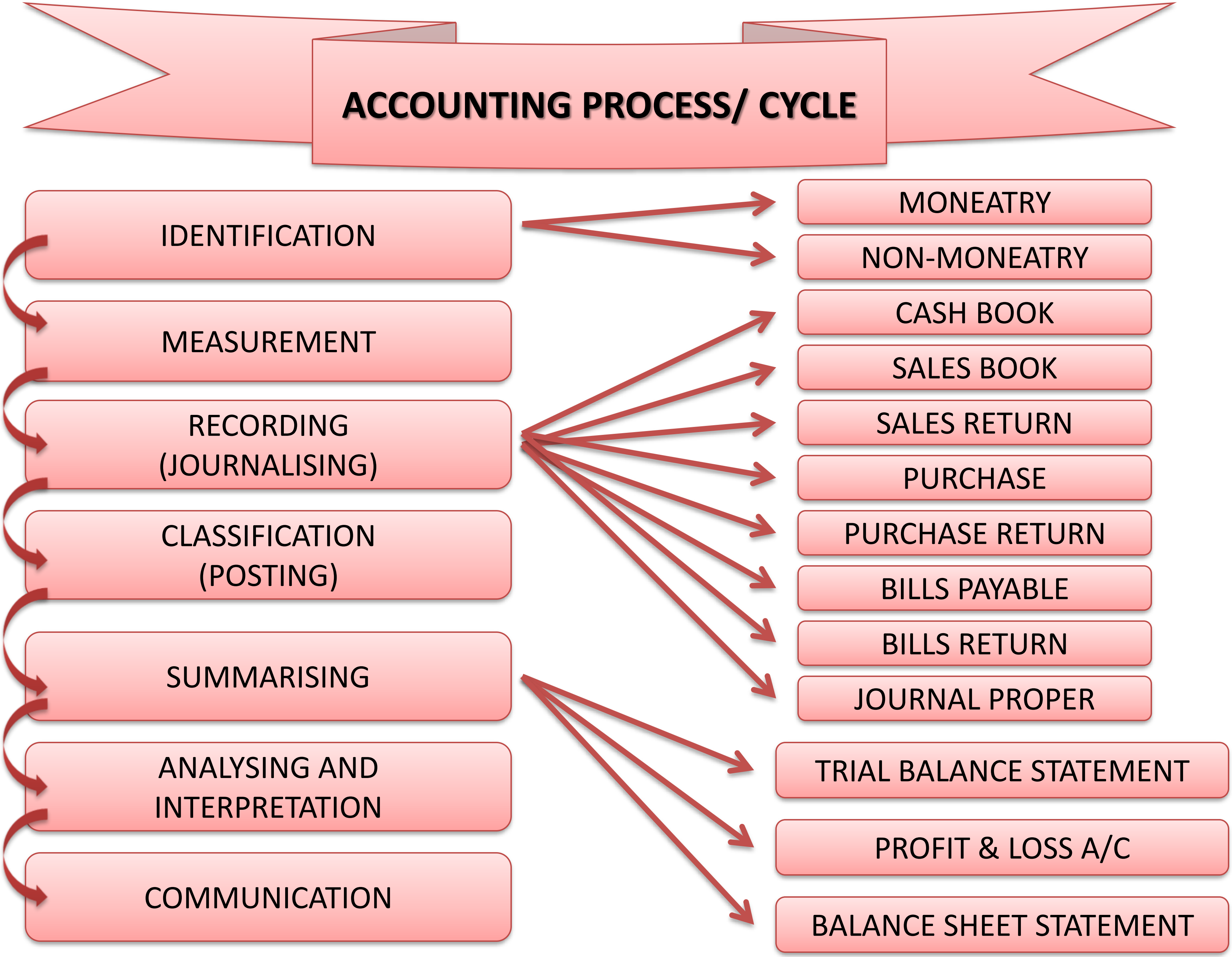
## Dr. And Cr. Rule

- **PERSONAL A/C:** Debit the receiver, Credit the giver
- **REAL A/C:** Debit all the expenses & losses, Credit all the income & gains
- **NOMINAL A/c:** Debit what comes in, Credit what goes out

| | INCREASE | DECREASE |
|---|---|---|
| Assets | Dr | Cr |
| Liability | Cr | Dr |
| Capital | Cr | Dr |
| Income | Cr | Dr |
| Expenses | Dr | Cr |

# Steps in Accounting Process





ACCOUNTING PROCESS/ CYCLE
IDENTIFICATION
MEASUREMENT
RECORDING (JOURNALISING)
CLASSIFICATION (POSTING)
SUMMARISING
ANALYSING AND INTERPRETATION
COMMUNICATION
MONEATRY
NON-MONEATRY
CASH BOOK
SALES BOOK
SALES RETURN
PURCHASE
PURCHASE RETURN
BILLS PAYABLE
BILLS RETURN
JOURNAL PROPER
TRIAL BALANCE STATEMENT
PROFIT & LOSS A/C
BALANCE SHEET STATEMENT

## EXPLAINED ABOVE MENTIONED TERMS

**Identification:** It means to determine what transactions to record.

**Measurement:** It means quantification (including estimates) of business transactions into financial terms by using monetary unit.

**Recording:** It means recording the identified financial transactions in the books of accounts in monetary terms and in a chronological order.

**Classifying:** The classifying phase of accounting involves sorting and grouping similar items under the designated name, category or account. This phase uses systematic analysis of recorded data in which all transactions are grouped in one place.

## EXPLAINED ABOVE MENTIONED TERMS

**Summarizing:** involves posting from ledger to prepare a trial balance and then the items of trial balance are posted in profit and loss account from which we get the net profit of the firm.

**Analysis and Interpretation**: refers to a systematic and critical examination of the financial statements. It not only establishes cause and effect relationship among the various items of the financial statements but also presents the financial data in a proper manner

**Communication:** The information is regularly communicated through accounting reports. These reports provide information that are useful to a variety of interested users.

# FORMAT OF PROFIT & LOSS A/C AND BALANCE SHEET

## BALANCE SHEET

Balance Sheet of ............ As at.............

| Liabilities | Rs. | Assets | Rs. |
|---|---|---|---|
| | | Fixed Assets: | |
| Capital: | | Good will | |
| Opening Balance xxxx | | Land | |
| Add: Net Profit xxxx | | Building | |
| (Less: Net Loss) | | Plant & Machinery | |
| Less: Drawings xxxx | | Furniture & Fixtures | |
| Long-term Liabilities: | | Investment: | |
| Loan | | Current Assets: | |
| Current liabilities: | | Closing stock | |
| Income received-in-advance | | Accrued income | |
| Sundry Creditors | | Prepaid expenses | |
| Outstanding Expenses | | Sundry Debtors | |
| Bills Payable | | Bills Receivable | |
| Bank Overdraft | | Cash at Bank | |
| | | Cash in Hand | |

# PROFIT & LOSS A/C

Dr. **Profit and loss account for the year ended .......** Cr.

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Gross loss b/d | xxx | By Gross profit b/d | xxx |
| To Office and administrative expenses: | | By Indirect incomes: | |
| Salaries | xxx | Rent earned | xxx |
| Rent, rates and taxes | xxx | Discount received | xxx |
| Printing and stationery | xxx | Commission earned | xxx |
| Postage | xxx | Interest on investments | xxx |
| Legal charges | xxx | Dividend on shares | xxx |
| Audit fees | xxx | Bad debts recovered | xxx |
| Establishment expenses | xxx | Profit on sale of fixed assets | xxx |
| Trade expenses | xxx | Apprenticeship premium | xxx |
| General travelling expenses | xxx | Miscellaneous receipts | xxx |
| Lighting | xxx | By Net loss* | xxx |
| Insurance premium | xxx | (transferred to capital account) | |
| To Selling and distribution expenses: | | | |
| Carriage outwards | xxx | | |
| Advertisement | xxx | | |
| Commission | xxx | | |
| Brokerage | xxx | | |
| Bad debts or provision for bad debts | xxx | | |
| Export duty | xxx | | |
| Packing charges | xxx | | |
| To Other expenses and losses: | | | |
| Repairs | xxx | | |
| Depreciation | xxx | | |
| Interest charges | xxx | | |
| Discount allowed | xxx | | |
| Provision for discount on debtors | xxx | | |
| Bank charges | xxx | | |
| Interest on capital | xxx | | |
| Donation and charity | xxx | | |
| Loss on sale of fixed assets | xxx | | |
| Abnormal loss due to fire, theft etc. not covered by insurance | xxx | | |
| To Net profit* | xxx | | |
| (transferred to capital account) | | | |
| | xxx | | xxx |

* The balance will be either net profit or net loss.

# THANK YOU