

Chapter 1 Meaning and Objectives of Accounting

Question 1

Define Accounting.

Answer:

Accounting can be defined as a process of reporting, recording, interpreting, and summarizing economic data. The introduction of accounting helps the decision-makers of a company to make effective choices, by providing information on the financial status of the business. Today, accounting is used by everyone and a good understanding of it is beneficial to all. Accountancy act as a language of finance.

Question 2

Distinguish between debtors and creditors.

Answer: Debtors are the persons who owe an amount to the enterprise for the goods sold or service provided to them on credit, whereas, creditors are the person who is to be paid an amount by the enterprise for buying from then goods and services on credit.

Question 3

What is a cash discount?

Answer: When a discount is allowed to the customer for making prompt payment it is called cash discount. It is always recorded in the books of account.

Question 4

Distinguish between debtors and creditors.

Answer: Debtors are the persons who owe an amount to the enterprise for the goods sold or service provided to them on credit, whereas, creditors are the person who is to be paid an amount by the enterprise for buying from then goods and services on credit.

Question 5

How is profit or loss of a specific term determined?

Answer: Profit or loss of a specific term determined by formulating loss account and trading and profit.

Question 6

How is the final position of a firm established?

Answer: The final position of a firm established by a balance sheet.

Question 7

Name the branch of commerce, which keeps a record of monetary transactions in a set of books.

Answer: Book-keeping is the branch of commerce, which keeps a record of monetary transactions in a set of books.

Question 9

Give one point of distinction between book-keeping and accountancy.

Answer: Book-keeping objective is to keep a transaction of a business in a systematic manner, whereas, accounting determines the profit or loss and the financial status of a firm.

Question 10

What is the end product of financial accounting?

Answer: The end product of accounting is the financial statement (i.e, profit and loss account and balance sheet) and reports which gives information to users about the financial position and profitability of an enterprise.

Question 11

Name any two users of accounting information.

Answer: The two users of accounting information are owners and Creditors.

Question 12

Who are the internal users of accounting information?

Answer: The internal users of accounting information are people who are directly involved in managing and operating the business enterprise such as directors or partners, managers, and officers.

Question 13

Who are the external users of accounting information?

Answer: The internal users of accounting information are potential investors, creditors, lenders, employee unions, customers, government, etc.

Question 14

State the nature of information required by investors.

Answer: The nature of information required by investors are regarding risks and return on investment in the business enterprise.

Question 15

What are the types of information required by long-term investors?

Answer: The type of information required by long-term investors are the creditworthiness and the ability of the enterprise to pay interest and the repayment of the loans.

Question 16

What are the information needs of management?

Answer: The information needs of management are timely information regarding sales, costs, profitability, etc. used for planning, controlling, and decision making.

Question 17

Mention two advantages of accounting.

Answer: The two advantages of accounting are

- (i) It provides a complete and systematic record
- (ii) It provides information regarding profit or loss

Question 18

Write one limitation of accounting.

Answer: The accounts are prepared on the basis of historical costs and as such the figures given in the financial statements do not show the effect of changes in the price level.

Question 19

Write the name of two qualitative characteristics of accounting information

Answer: The name of two qualitative characteristics of accounting information are reliability and comparability.

Question 20

Which qualitative characteristic of accounting information requires the use of common unit and format of reporting?

Answer: The qualitative characteristic of accounting that requires the use of common unit and format of reporting is comparability.

Question 21

'Accounting information should be verifiable and free from personal Bias'. Name the qualitative characteristics of accounting information denoted by this statement.

Answer: The qualitative characteristic of accounting information denoted by this statement is reliability.

Question 22

Name the two functions of accounting.

Answer: The two functions of accounting are.

- (i) Maintaining systematic accounting records
- (ii) Preparation of financial statement

Question 23

What is the traditional function of accounting?

Answer: The traditional function of accounting is to record financial transactions

Question 24

Explain the characteristics of Accounting.

Answer: A few characteristics of Accounting are.

- **Accounting is an art as well as science-** Accounting can be defined as an art as it has a technique to pre-determines object. It records, classifies, and summarizes all the transactions of a company, to determine the net profit and financial status of the business. Secondly, it can also be compared to science as it an organized body that is based on a particular principle and accounting standard.
- **Recording of Financial Transaction only-** In accounting, only transactions or items related to the financial character are recorded.
- **Recording in terms of Money-** In business, anything that is not related to money does not record in accounting.

- **Classifying-** Once the recording is done in a journal or any subsidiary book, the transactions are then classified. Here classification means segregating one type of transaction in one place and separate accounts. The book in which each type of transaction is recorded according to its nature is known as Ledger.
- **Summarizing-** It is a process where all the classified transactions are presented in such a way that it is understandable and useful to the management and other users.
- **Interpretation of the Results-** Accounting summarizes the result of a company in such a way that it gives full and detailed information about the profits and financial status of a company to the bank, employees, investors, creditors, etc.
- **Communicating-** Accounting also gives a progress report of a company to the users and examines them according to their requirements.

Higher-Order Thinking Skills (HOTS) Questions

Question 1

What is the traditional function of accounting?

Answer: The traditional function of accounting is a recording of a financial transaction.

Question 2

Is the basic objective of book-keeping to maintain systematic records or to ascertain net results of operations of a financial transaction?

Answer: The basic objective of book-keeping to maintain systematic records or to ascertain net results of operations of a financial transaction is to maintain systematic records of financial transactions.

Question 3

Recording of financial transactions and preparing financial statements are the only objectives of accounting. Do you agree?

Answer: No, besides these two, accounting has the objective of providing useful information to the management and communication of financial information to the users.

Question 4

What is the first step in the accounting process?

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

Question 5

What is the last step of the accounting process?

Answer: The last step of the accounting process is communicating the final results to the users who analyzes them as per their individual requirement.

Question 6

On 1st Jan. 2015, Mr Vadera was appointed as marketing manager in a company with ₹50,000 per month salary. Explain whether this case will be registered in the book of accounts.

Answer: No, the appointment will not be recorded because it has not resulted in any change in the financial position of the firm (It will be recorded only when the salary is paid)

Question 7

A company follows a practice of giving the figures for the previous year along with the figures of the current year. Now the accountant of the firm wants to discontinue this practice. Do you justify this decision?

Answer: No, the comparability of current year figures with that of the previous year is a qualitative characteristic of financial information. Discontinuation of this practice will result in discontinuation of a good practice being followed by the firm.

Question 8

Give two examples of transactions that are not recorded in accounting.

Answer: The two examples of transactions that are not recorded in accounting are (i) Resignation by the general manager (ii) Value of human resources.

Question 9

A firm has received a large order to supply the goods. Will it be recorded in the books?

Answer: No, only the receipt of an order has not resulted in any change in the financial position of the firm.

Value-Based Questions

Question 1

What is the value involved in giving the figures of the previous year along with the figures of the current year in financial statements?

Answer: Giving the figures for the previous year along with the figures of the current year facilitates a comparison of current performance with past performance.

Question 2

Mr. Ganpati, the proprietor of a business, sold his residential house of ₹50 lac. Will it be recorded in the books of account?

Answer: No, personal dealings of the proprietor are not recorded in the books of the firm. However, if he invests this amount in the business it will be treated as additional capital introduced by the proprietor and then it will be recorded in books of the firm.

Question 3

What is the value involved in giving explanatory notes with the financial statements?

Answer: Explanatory notes explain the information given in financial statements which makes them more useful and understandable.

Question 4

The principal of a public school conducted an interview of candidates for selection of an accountancy teacher. Miss Arun was selected and was given an appointment letter wherein her salary was stated as ₹30,000 per month. Will it be recorded in the books of accounts?

Answer: No, only the selection of a teacher is not of financial character. It will be recorded when the salary is actually disbursed.

Question 5

What is the value involved in adopting the same method of depreciation year after year?

Answer: The value involved in adopting the same method of depreciation year after-after is comparability. Comparability is possible when a firm adopts the same method of depreciation year after year.

Question 6

Miss Priti, an electronic goods dealer, gifted a washing machine valued ₹25,000 to her friend Suruchi. Will it be recorded in the books of account?

Answer: Yes, it will be treated as drawings of Miss. Priti and will be recorded in the books.

Question 7

How is accounting influenced by personal judgment?

Answer: Accounts has to exercise his personal judgment in respect of various items. For example, it is extremely difficult to predict with any degree of accuracy the actual useful life of an asset which is needed for calculating depreciation. The same is true about the method of valuation of stock and making provision for doubtful debts.

Question 8

Mr. Vishwanath established a travel agency. Over the travel agency earned a high reputation. Mr. Vishwanath Considers the value of goodwill of his travel agency at ₹50 lakhs. He wants to record the value of the goodwill in the books of accounts. Can he do so?

Answer: No, only the purchased goodwill can be recorded in the books of accounts. 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.

Question 9

Land and buildings are shown at 10 lakhs in the balance sheet of the business owned by Mr. Yuvraj. However, as per the certificate of a government-approved valuer, the realizable value of land and building is ₹200 lakhs. Mr. Yuvraj wants to show the land and building at this value in his books. Can he do so?

Answer: No, accounts are maintained on the concept of historical cost (i.e, the original cost). According to this concept, an asset is recorded in the books of accounts at the price at which it was acquired.

Question 10

What is meant by qualitative information?

Answer: Qualitative aspects of business units are those aspects which cannot be expressed in monetary terms, such as changes in management, the reputation of the business, cordial management-labour relations, firm's ability to develop new products, the efficiency of management, a satisfaction of firm's customers, etc.

Question 11

What is meant by 'window dressing' in accounting?

Answer: Window dressing refers to the practice of manipulating accounts so that the financial statements may disclose a more favorable position than the actual position. For example, the purchases made at the end of the year may not be recorded or the closing stock may be over-valued.

Question 12

The huge loss occurred due to the strike of the employee. Will it be recorded?

Answer: No, because only those transactions and events are recorded in accounting which are of a financial character and the effect of which can be measured in terms of money.

Question 13

If the accounting information is not clearly presented, which of the qualitative characteristics of the accounting information is violated?

Answer: If the accounting information is not clearly presented, then the understandability characteristics of the accounting information is violated.

Question 14

Confidence trust that the reported information is a reasonable representation of the actual items and events, that have occurred, depicts which qualitative characteristic of accounting information.

Answer: It depicts the reliability characteristic of accounting information.

Question 15

Identify the value being violated in case of window dressing.

Answer: The values being violated in case of window dressing are.

(i) Honesty – By not showing the true and fair view of the result of operations and financial position of the enterprises, management is not honest towards the users of financial statements.

(ii) Transparency – Business has violated the value of transparency.

Question 16

Which value is most important for a good accountant?

Answer: A good accountant is the one who is honest and shrewd. He must ensure that all transactions are recorded in the books of accountants and there should be no hiding of facts. Sometimes, pressure may be put on him to hide certain facts in accounts to evade tax or any other purpose. But he should behave in an honest and shrewd manner.

Question 17

The accountant of the firm found an error in the books of account but neither he rectified the error nor disclosed it to the management fearing that it will risk his job. Which value has been violated by the accountant?

Answer: The accountant has violated the value of honesty and trust.

Question 18

Accounting records business transactions and events which are of financial nature. Do you consider it a limitation of accounting?

Answer: Yes, it is a limitation of accounting because there are events that have a vital bearing on the profitability of the firm and such events are ignored.