IARE '24 DISCORD TEAM

II-II

BEFA MODULE 5 SOLUTIONS

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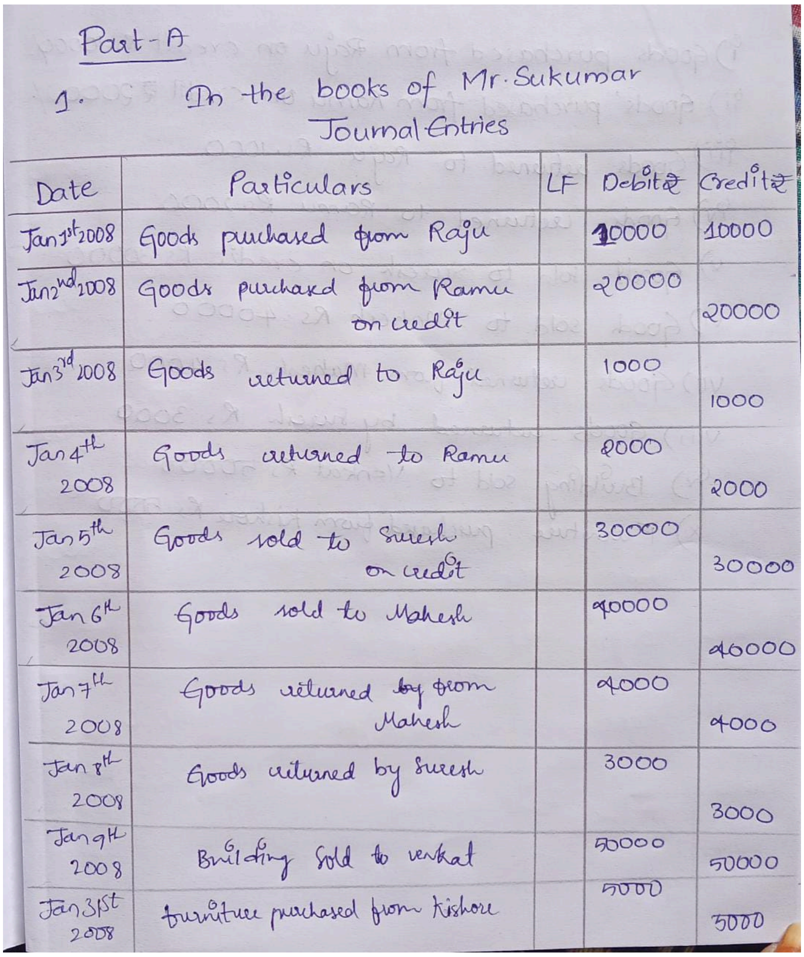
INTRODUCTION TO FINANCIAL ACCOUNTING AND FINANCIAL ANALYSIS

Completed

BEFA MODULE 5

PART A (3 Done, Remaining Same Pattern)

1. Write Journal Entries in the books of Mr. Sukumar from the following transactions 2008, Jan.1st Goods purchased from Raju on credit Rs. 10,000 Jan 2nd Goods purchased from Ramu Rs. 20,000 Jan 3rd Goods returned to Raju Rs. 1,000 Jan 4th Goods returned to Ramu Rs. 2,000 Jan 5th Goods sold to Suresh on credit Rs. 30,000 Jan 6th Goods sold to Mahesh Rs. 40,000 Jan 7th Goods returned from Mahesh Rs. 4,000 Jan 8th Goods returned by Suresh Rs. 3,000 Jan 9th Building sold to Venkat Rs. 50,000 Jan 31st Furniture purchased from Kishore Rs.5,000.



Part-A

1. In the books of Mr. Sukumar

Journal Entries

Date	Particulars	LF	Debit₹	Credit₹
Jan 1st 2008	Goods purchased from Raju		10000	10000
Jan 2nd 2008	Goods purchased from Ramu on credit		20000	20000
Jan 3rd 2008	Goods returned to Raju		1000	1000
Jan 4th 2008	Goods returned to Ramu		2000	2000
Jan 5th 2008	Goods sold to Suresh on credit		30000	30000
Jan 6th 2008	Goods sold to Mahesh		40000	40000
Jan 7th 2008	Goods returned ~~by~~ from Mahesh		4000	4000
Jan 8th 2008	Goods returned by Suresh		3000	3000
Jan 9th 2008	Building sold to venkat		50000	50000
Jan 31st 2008	furniture purchased from Kishore		5000	5000

2. Write Journal Entries in the books of Mr. Bhavani Sankar from the following transactions 2002, Jan.1st Business commenced with Rs. 15,000 Jan.2nd. Cash paid into bank Rs. 10,000 Jan. 3rd. Sold goods for cash Rs. 7,000 Jan.

4th. Purchased goods from Vijay Rs. 3,000 Jan. 5th. Machinery Purchased for Rs. 5,000 Jan.30th Rent paid Rs. 2,000 Jan 31st Depreciation charged on Machinery Rs. 3,000 Jan 31st Depreciation charged on Furniture Rs.500.

(2) In the books of Mr. Bhavani Sankar

Journal Entries.

Date	Particulars	LF	Debit ₹	Credit ₹
Jan 1, 2002	Bhavani Sankar commenced business with cash		15000	15000
Jan 2, 2002	Cash paid into bank		10000	10000
Jan 3, 2002	Sold goods for cash		7000	7000
Jan 4, 2002	Purchased goods from Vijay		3000	3000
Jan 5, 2002	Machinery purchased		5000	5000
Jan 30, 2002	Rent paid		2000	2000
Jan 31, 2002	Depreciation charged on Machinery		3000	3000
Jan 31, 2002	Depreciation charged on furniture		5000	5000

3. Prepare Journal Entries in the books of Mr. Kiran from the following transactions and write ledger accounts. 2013, May 1st Insurance paid by cheque Rs.3,000 May 9th Telephone Rent Paid in cash Rs.2,000 May 10th Stationery Purchased for Rs.1,000 May 11th Telegrams sent to New Delhi Rs.2,500 May 12th Advertisement charges paid in cash Rs.5,000 May 13th Machinery Purchased for Rs.90,000 May 14th Furniture purchased for

personal use Rs.30,000 May 13th Depreciation charged on Machinery Rs.9,000 May 14th Depreciation charged on Furniture Rs.3,000 May 15th Repairs Paid on Buildings Rs.15,000 May 16th Rent received for Rs.6,000.

③ In the books of Mr. Kiran Journal Entries.

Date	Particulars	L.F	Debit ₹	Credit ₹
May 1, 2013	Insurance paid by cheque		3000	3000
May 9, 2013	Telephone rent paid in cash		2000	2000
May 10, 2013	Stationery Purchased		1000	1000
May 11, 2013	Telegrams sent to New Delhi		2500	2500
May 12, 2013	Advertisement Charges paid in cash		5000	5000
May 13, 2013	Machinery Purchased		90000	90000
May 14, 2013	Furniture Purchased for personal use		30000	30000
May 13, 2013	Depreciation charged on Machinery		9000	9000
May 14, 2013	Depreciation charged on furniture		3000	3000
May 15, 2013	Repairs paid on Buildings		15000	15000
May 16, 2013	Rent recieved		6000	6000

10) Similar question below

From the following ledger balances prepare trial balance :
Capital ₹ 20,800, Rent outstanding ₹ 1,420, Amount due to Param, ₹ 15,000, Drawing ₹ 2,800, Goodwill ₹ 12,000, Interest received ₹ 2,000, Discount received ₹ 1,580, Amount due from Deepan ₹ 26,000.

Solution

Trial Balance

Name of Accounts	L.F.	Debit Balance (Rs)	Credit Balance (Rs)
Capital			20,800
Outstanding Rent			1,420
Due to Param			15,000
Drawings		2,800	
Goodwill A/c		12,000	
Interest Received			2,000
Discount Received			1,580
Due from Deepan		26,000	
Total		**40,800**	**40,800**

PART B

1. Define Financial Accounting. Explain the importance and Limitations of Financial Accounting.

Financial Accounting concerns with providing information to external users. It refers to the preparation of general-purpose reports for use by persons outside a business enterprise, such as shareholders (existing and potential), creditors, financial analysts, labour unions, government authorities, and the like. Financial accounting is oriented towards the preparation of financial statements which summarise the results of operations for selected periods of time and show the financial position of the business at particular dates.

Importance of Financial Accounting:

Financial accounting is integral to companies of all sizes because it helps in the following importance below: They are three important points.

Communication of information externally.

The statements and reports generated by financial accounting are used to communicate information about the overall health and well-being of the company to external parties. Such external users may include suppliers, banks, leasing companies, etc. who are not part of the company but require all this information to analyse the progress of the company and compare it with their expectations.

Communicate information internally

A company's finance team or its employees who are interested in stock-based compensation etc. constitute the internal users of the information generated by financial accounting practices. The reports generated with the help of financial accounting skills are helpful for this purpose as well.

Comparison through analysis

Since financial accounting requires the use of standardised guidelines, the financial statements generated by all companies are comparable, providing a standard method of analysis.

Limitations of Financial Accounting:

- Does not record all events: Only the transactions of a financial character will be recorded under book-keeping. So it does not reveal a complete picture about the quality of human resources, locational advantage, business contacts etc.
- Does not reflect current values: The data available under book-keeping is historical in nature. So they do not reflect current values. For instance, we record the value of stock at cost price or market price, whichever is less. In case of building, machinery etc., we adopt historical cost as the basis. Infact, the current values of buildings, plants and machinery may be much more than what is recorded in the balance sheet.
- Estimates based on Personal Judgement: The estimate used for determining the values of various items may not be correct. For example, debtors are estimated in terms of collectibility, inventories are based on marketability, and fixed assets are based on useful working life. These estimates are based on personal judgement and hence sometimes may not be correct.
- Inadequate information on costs and Profits: Book-keeping only provides information about the overall profitability of the business. No information is given about the cost and profitability of different activities of products or divisions

2. Explain with examples how you would use ratio analysis to understand financial statements?

Ratio Analysis Absolute figures are valuable but they standing alone convey no meaning unless compared with another. Accounting ratio show inter-relationships which exist among various accounting data. When relationships among various accounting data supplied by financial statements are worked out, they are known as accounting ratios.

Ratio Analysis: Ratio is an expression of one number that is related to another. It is one of the methods of analysing financial statements. Ratio analysis facilities the presentation of the information of the financial statements are simplified and summarised from. Ratio is a measuring of two numerical positions. It expresses the relation between two numeric figures.

The following are the main uses of Ratio analysis:

(i) Useful in financial position analysis: Accounting reveals the financial position of the concern.

This helps banks, insurance companies and other financial institutions in lending and making investment decisions.

(ii) Useful in simplifying accounting figures: Accounting ratios simplify, summaries and systematic the accounting figures in order to make them more understandable and in lucid form.

(iii) Useful in assessing the operational efficiency: The efficiency of the firm becomes evident when analysis is based on accounting ratio. This helps the management to assess financial requirements and the capabilities of various business units.

(iv) Useful in forecasting purposes: If accounting ratios are calculated for a number of years, then a trend is established. This trend helps in setting up future plans and forecasting.

(v) Useful in locating the weak spots of the business: Accounting ratios are of great assistance

3. Define Account. Illustrate different types and principles of Accounts (Rules of Debit and Credit).

In banking, an account refers to an arrangement by which a financial institution accepts a customer's financial assets and holds them on behalf of the customer at his or her discretion.
Three classes of accounts are maintained for recording all business transactions.
They are:
1.Personal accounts
2.Real accounts
3.Nominal accounts
1. Personal Accounts: Accounts which are transactions with persons are called “Personal Accounts” .A separate account is kept on the name of each person for recording the benefits received from ,or given to the person in the course of dealings with him.
2. Real Accounts: The accounts relating to properties or assets are known as “Real Accounts”..A separate account is maintained for each asset owned by the business.
E.g.: cash A/C, furniture A/C, building A/C, machinery A/C etc
3. Nominal Accounts: Accounts relating to expenses, losses, incomes and gains are known as “Nominal Accounts”. A separate account is maintained for each item of expenses, losses, income or gain.

Accounting is the process of recording financial transactions pertaining to a business. The accounting process includes summarising, analysing, and reporting these transactions to oversight agencies, regulators, and tax collection entities.
Every business transaction which can be measured in monetary terms finds a place in the accounting transactions of a firm. In order to record such transactions, a system of debit and credit has been devised, which records such events through two different accounts.
The net effect of these accounting entries is the same in terms of quantity. However, by debiting and crediting two different accounts, the correct and apt accounting treatment can be depicted.

- A **debit** is an accounting entry that either increases an asset or expense account. Or decreases a liability or equity account. It is positioned on the left in an accounting entry.

- A **credit** is an accounting entry that increases either a liability or equity account. Or decreases an asset or expense account. It is positioned on the right in an accounting entry.
- Whenever an accounting transaction happens, a minimum of two accounts is always impacted, with a debit entry being recorded against one account and a credit entry being recorded against another account. There is no upper limit to the number of accounts involved in a transaction but the minimum cannot be less than two accounts.
- The totals of the debits and credits for any transaction must always equal each other so that an accounting transaction is always said to be in balance. Thus, the use of debits and credits in a two column transaction recording format is the most essential of all controls over accounting accuracy. This is how debit and credit find their use.

The following are the rules of debit and credit which guide the system of accounts, they are known as the Golden Rules of accountancy:

- First: Debit what comes in, Credit what goes out.
- Second: Debit all expenses and losses, Credit all incomes and gains.
- Third: Debit the receiver, Credit the giver.

4. Define Double Entry System. Describe the advantages and Disadvantages of the Double Entry System.

Double entry system of booking is an accounting system which recognizes the fact that every transaction has two aspects and both aspects of the transaction are recorded in the books of accounts. In other words, it recognizes that in order to receive some value, an equal value needs to be given.

Advantages of double entry system

- In contrast to a single entry, this is a scientific method of tracking business transactions. It assists in the rechecking and cross-checking of accounting documents.
- Both sides of a transaction are registered as debit and credit in this system, so we keep separate accounts for the purchase and payment.
- When we pass an entry on both sides, the account is automatically reviewed in this method. We will quickly find the error if both sides of the trial balance are not balanced.

- The profit and loss account indicates how much profit or loss was made over a given time.
- As long as we have the accounting books, we can analyse the profit and loss report and balance sheet of any two or more years.
- Since any transaction has two records, misappropriations and frauds can be easily identified.
- We will calculate the financial status of the company at the end of the year by preparing a profit and loss report and a balance sheet.

Disadvantages of double entry system

- The double-entry system is complex in nature since it must respond to various accounting standards and principles.
- Maintaining accounting books takes more time, which necessitates the recruitment of more staff, leading to a cost increase.
- Since their fees are too high, small companies cannot afford to hire anyone with proper accounting skills.
- Every transaction must be documented twice, resulting in larger books or the need for a more efficient computer to process data in electronic form.

5. Outline the significance of Trial Balance. Sketch different methods of preparing Trial Balance.

A trial balance is a statement of debit and credit balances. It is prepared on a particular date with the object of checking the accuracy of the books of accounts. It indicates that all the transactions for a particular period have been duly entered in the book, properly posted and balanced. The trial balance doesn't include stock in hand at the end of the period. All adjustments required to be done at the end of the period including closing stock are generally given under the trial balance.

There are three methods in which a Trial Balance can be prepared. Which are as follows :

- Total Method or Gross Trial Balance
- Balance Method or Net Trial Balance
- Compound Method

Total Method or Gross Trial Balance:

Under this method, two sides of the accounts are totaled. The total of the debit side is called the "debit total" and the total of the credit side is called the "credit total". All the debit totals are entered on the debit side of the Trial Balance while the credit total is entered on the credit side of the Trial Balance

If any particular account has a total on one side, it will be entered either in the debit column or the credit column as the case may be.

Advantage

- It promotes the arithmetical accuracy of the accounts.
- Extraction of ledger balances is not required at the time of preparation of Trial Balance.

•Net Trial Balance or Balance Method:

Under this method, all the ledger accounts are balanced. The balancing figure may be either a "debit balance" or "credit balance".

Advantage

o It helps in the easy preparation of final accounts.

o Time and labour can be saved in constructing a Trial Balance following this method.

- Compound Method:

Under this method, totals of both the sides of the accounts are written in the separate columns. Along with this, the balances are also written in the separate columns. Debit balances are written in the debit column and credit balances are written in the credit column of the Trial Balance.

Advantage

o It offers the advantage of both methods.

6. List out different types of Accounting Concepts and Conventions.

Accounting is a system evolved to achieve a set of objectives. In order to achieve the goals, we need a set of rules or guidelines. These guidelines are termed here as "BASIC ACCOUNTING CONCEPTS". The term concept means an idea or thought. Basic accounting concepts are the fundamental ideas or basic assumptions underlying the theory and profit of FINANCIAL ACCOUNTING.

These concepts help in bringing about uniformity in the practice of accounting. In accountancy following concepts are quite popular.

1. BUSINESS ENTITY CONCEPT: In this concept “Business is treated as separate from the proprietor”. All the Transactions recorded in the book of Business and not in the books of proprietor. The proprietor is also treated as a creditor for the Business.

2.GOING CONCERN CONCEPT: This concept relates with the long life of Business. The assumption is that business will continue to exist for an unlimited period unless it is dissolved due to some reasons or the other.

3.MONEY MEASUREMENT CONCEPT: In this concept “Only those transactions are recorded in accounting which can be expressed in terms of money, those transactions which can not be expressed in terms of money are not recorded in the books of accounting”.

4.COST CONCEPT: Accounting to this concept, an asset is recorded at its cost in the books of account. i.e., the price, which is paid at the time of acquiring it. In the balance sheet, these assets appear not at cost price every year, but depreciation is deducted

5.ACCOUNTING PERIOD CONCEPT: every Businessman wants to know the result of his investment and efforts after a certain period. Usually a one-year period is regarded as an ideal for this purpose. This period is called the Accounting Period. It depends on the nature of the business and the object of the proprietor of the business.

6.DUAL ASPECT CONCEPT: According to this concept “Every business transactions has two aspects”, one is the receiving benefit aspect another one is giving benefit aspect. The receiving benefit aspect is termed as “DEBIT”, whereas the giving benefit aspect is termed as “CREDIT”. Therefore, for every debit, there will be corresponding credit.

ACCOUNTING CONVENTIONS

Accounting is based on some customs or usages. Naturally accountants here adopt that usage or custom. They are termed as convert conventions in accounting. The following are some of the important accounting conventions.

1.FULL DISCLOSURE: According to this convention accounting reports should disclose fully and fairly the information. They purport to represent. They should be prepared honestly and sufficiently disclose information which is if material interest to proprietors, present and potential creditors and investors.

2.MATERIALITY: Under this convention the trader records important factor about the commercial activities.

3.CONSISTENCY: It means that the accounting method adopted should not be changed from year to year. It means that there should be consistency in the methods or principles followed. Or else the results of a year cannot be conveniently compared with that of another.

4. CONSERVATISM: This convention warns the trader not to take unrealized income into account. That is why the practice of valuing stock at cost or market price, whichever is lower, is vague. This is the policy of “playing safe”; it takes into consideration all prospective losses but leaves all prospective profits.

7. Summarise the importance of Balance Sheets. Draw the Performa of Balance sheet & Major involvements.

The term balance sheet refers to a financial statement that reports a company's assets, liabilities, and shareholder equity at a specific point in time. Balance sheets provide the basis for computing rates of return for investors and evaluating a company's capital structure.

The importance of balance sheet.

1. It helps in checking the arithmetical accuracy of books of accounts.
2. It helps in the preparation of financial statements.
3. It helps in detecting errors.
4. It serves as an instrument for carrying out the job of rectification of entries.
5. It is possible to find out the balances of various accounts at one place.

BALANCE SHEET OF .... AS ON...

TABLE 5.4: Trading and Profit and Loss Account

Liabilities	Amount	Assets	Amount
Creditors Bills payable	XXXX	Cash in hand	XXXX
Bank overdraft	XXXX	Cash at bank	XXXX
Loans	XXXX	Bills receivable	XXXX
Mortgage	XXXX	Debtors	XXXX
Reserve fund		Closing stock	XXXX
Capital xxxxxx		Investments	XXXX
Add: Net Profit		Furniture and fittings	XXXX
Less: Drawings	XXXX	Plats&machinery	XXXX
		Land & buildings	XXXX
		Patents, tm ,copyrights Goodwill	XXXX
		Prepaid expenses	XXXX
		Outstanding incomes	XXXX
	XXXX		XXXX

8. List out the advantages of the Journal. and Illustrate the importance of the ledger.

Advantages of the Journal

Journalizing the business transaction is done by the majority of businesses. Journal helps a business to keep a systematic record of its financial events. To know the advantages of maintaining the same, we can sum it in the following points:

- Journal records all the financial transactions of a business in one place on a time and date basis.
- The transactions are recorded, in support of a bill, to check the authenticity of each of these journal entries with their bills.
- There is less chance to avoid transactions as in a journal we record every transaction on a date basis.
- The accountant writes each journal entry's narration below every journal entry so that another auditor can audit it without any confusion.

- In a journal, we record these transactions which help in the deep analysis of the two accounts based on a double-entry system, and this prevents a minimum chance of mistake in the journal.
- Journal posts the transactions in their respective ledger accounts. Without making this journal, an accountant will be unable to make the ledger accounts.
- In case of a mistake in the ledger accounts, this can be easily rectified with the help of a journal or by passing a rectified journal entry in the journal.

The importance of the ledger:

1. Each account in Ledger will have separate headings.
2. Account transactions are recorded in a specific table.
3. Transactions are recorded on the account by date.
4. Each ledger has a column of two amounts. The amount of the transaction in both columns is written by debit and credit.
5. There is a column to write the ref number on both sides of the account.
6. The balance of the account is calculated at the end of the period.
7. After completion of the calculation, the Debit and Credit Column is closed by drawing two parallel lines below the sum of both sides.

9. What do you mean by final accounts? What are its constituents? Name them and briefly explain the purpose of each of them.

In every business, the business man is interested in knowing whether the business has resulted in profit or loss and what the financial position of the business is at a given time. In brief, he wants to know

(i)The profitability of the business and

(ii) The soundness of the business.

The trader can ascertain this by preparing the final accounts. The final accounts are prepared from the trial balance. Hence the trial balance is said to be the link between the ledger accounts and the final accounts. The final accounts of a firm can be divided into two stages. The first stage is preparing the trading and profit and loss account and the second stage is preparing the balance sheet.

Trading account

A trading account shows the results of the buying and selling of goods. This sheet is prepared to demonstrate the difference between the selling price and the cost price. The trading account is prepared to show the trading results of the business, example. gross profit earned or gross loss sustained by the business. It records the direct expenses of a business firm.

Profit and loss account

This account is prepared to ascertain the net profit/loss and expenses of a business during an accounting year.It records the indirect expenses of a business firm, like rent, salaries, and advertising expenses. Profit and loss a/c includes expenses and losses as well as income and gains, which have occurred in business other than the production of goods and services.

Balance sheet

The balance statement demonstrates the financial position of a business on a specific date. The financial position of a business is found by tabulating its assets and liabilities on a particular date. The excess of assets over liabilities represents the capital sunk into the business and reflects the financial soundness of a company.

10. Explain the significance of Trial Balance. Sketch different methods of preparing Trial Balance.

Trial balance helps in locating errors by providing a starting point for the location of errors committed if any. * Trial balance provides a basis for the preparation of final accounts. Under the total method, trial balance is prepared by taking up the total of debits and credit of all ledger accounts.

- Total Method or Gross Trial Balance:

Under this method, two sides of the accounts are totaled. The total of the debit side is called the "debit total" and the total of the credit side is called the "credit total". All the debit totals are entered on the debit side of the Trial Balance while the credit total is entered on the credit side of the Trial balance.

Advantage • It promotes the arithmetical accuracy of the accounts.

- Extraction of ledger balances is not required at the time of preparation of Trial Balance.

Disadvantage • Preparation of final accounts is not possible.

- Net Trial Balance or Balance Method:

Under this method, all the ledger accounts are balanced. The balancing figure may be either a "debit balance" or "credit balance".

Advantage o It helps in the easy preparation of final accounts.

o Time and labour can be saved in constructing a Trial Balance following this method.

Disadvantage o Errors may remain undisclosed irrespective of the agreement of Trial Balance.

- Compound Method:

Under this method, totals of both the sides of the accounts are written in the separate columns. Along with this, the balances are also written in the separate columns. Debit balances are written in the debit column and credit balances are written in the credit column of the Trial Balance.

Advantage o It offers the advantage of both methods.

Disadvantage o Lengthy process and more time consumed in the preparation of a Trial Balance.

Q11.Explain the importance of Trading Account. Illustrate the significance of Profit & Loss Account.

A trading account shows the results of the buying and selling of goods. This sheet is prepared to demonstrate the difference between the selling price and the cost price. The trading account is prepared to show the trading results of the business, example. gross profit earned or gross loss sustained by the business. It records the direct expenses of a business firm.

Trading account of MR. . . . . for the year ended . . . .

Table 11: Trading and Profit and Loss Account

Particulars	Amount	Particulars	Amount
To opening stock	XXXX	By sales	XXXX
To purchases xxxx		Less: returns xx	
Less: returns xx	XXXX	By closing stock	XXXX
To carriage inwards	XXXX		
To wages	XXXX		
To freight	XXXX		
To customs duty, octroi	XXXX		
To gas, fuel, coal, Water	XXXX		
To factory expenses	XXXX		
To other man. Expenses	XXXX		
To productive expenses	XXXX		
To gross profit c/d	XXXX		

Finally, a ledger may be defined as a summary statement of all the transactions relating to a person , asset, expense or income which have taken place during a given period of time. The up-to-date state of any account can be easily known by referring to the ledger.

PROFIT AND LOSS ACCOUNT

The business man is always interested in knowing his net income or net profit.Net profit represents the excess of gross profit plus the other revenue incomes over administrative, sales, Financial and other expenses.

Profit and loss account

This account is prepared to ascertain the net profit/loss and expenses of a business during an accounting year.It records the indirect expenses of a business firm, like rent, salaries, and advertising expenses. Profit and loss a/c includes expenses and losses as well as income and gains, which have occurred in business other than the production of goods and services.

PROFIT AND LOSS A/C OF MR. . . . . .FOR THE YEAR ENDED. . . . . .

Table 12: Trading and Profit and Loss Account

Particulars	**Amount**	**Particulars**	**Amount**
To office salaries	XXXX	By By Gross profit b/d	XXXX
To rent,rates,taxes	XXXX	By By Interest received	XXXX
To Printing and stationery	XXXX	By By Discount received	XXXX
To Legal Charges	XXXX	By By Commission received	XXXX
To Audit fee	XXXX	By By Income from investments	XXXX
To Insurance	XXXX	By By Dividend on shares	XXXX
To General expenses	XXXX	By By Miscellaneous investments	XXXX
To Advertisements	XXXX	By By Rent received	XXXX
To Bad debts	XXXX		
To Carriage outwards	XXXX		
To Repairs	XXXX		
To Depreciation	XXXX		
To interest paid	XXXX		
To Interest on capital	XXXX		
To Interest on loans	XXXX		
To Discount allowed	XXXX		
To Commission	XXXX		
To Net profit → (transferred To capital a/c)	XXXX		
	XXXX		XXXX

Q12. Draw the Performa of Trading account, Profit & loss account and Major involvements

Draw The tables in Q11 for trading account and profit & loss account.

Performa for trading account

Trading account for the year ended..........

To opening stock		xxx	By Sales	xxxx	
To purchases	xxxx		Less returns	xx	
Less returns	xxx			--------	xxxx
	-------------	xxxx	By closing stock		xxx
To Direct expenses:			By gross loss (if loss)		xxx
Carriage inward		xxx			
Freight		xxx			
Octroi		xxx			
Dock dues		xxx			
Excise duty		xxx			
Royalty		xxx			
Motive power		xx			
Coal, gas, water		xxx			
Factory expenses		xxx			
To Gross Profit (if profit)		xxx			
		xxxxx			xxxxx

Performa for profit and loss account

Profit & Loss Account
(For the year ended...)

Dr. Particulars	Amount	Particulars	Cr. Amount
To Gross loss b/d	Xxx	By Gross Profit b/d	Xxx
To Salaries	Xxx	By Discount Received	Xxx
To Office rent, rates and taxes	Xxx	By Commission Received	Xxx
To Printing & stationery	Xxx	By Bank Interest	Xxx
To Telephone expenses	Xxx	By Rent received	Xxx
To Postage & telegram	Xxx	By Dividend on shares	Xxx
To Discount Allowed	Xxx	By Interest earned on debentures	Xxx
To Insurance	Xxx	By Profit on sale of asset	Xxx
To Audit Fees	Xxx	By Net loss	Xxx
To Electricity charges	Xxx		
To Repairs & renewals	Xxx		
To Depreciation	Xxx		
To Advertisement	Xxx		
To Carriage Outwards	Xxx		
To Bad Debts	Xxx		
To Provision for Bad debts	Xxx		
To Selling commission	Xxx		
To Bank Charges	Xxx		
To Interest on loans	Xxx		
To Loss on sale of asset	Xxx		
To Net Profit	Xxx		
	xxx		xxx

Q13. What is the Double Entry System? Describe the advantages and Disadvantages of the Double Entry System.

Advantages of Double Entry System

- Double Entry System is Scientific System: This is a scientific system for recording business transactions as compared to a single entry. It helps to recheck and counter check the books of accounts.

- Double Entry System Record Complete Transactions: In this system, both sides of a transaction are recorded as debit and credit, so we record both purchase and payment in different accounts.
- Recheck the Accounts: In this system, the account is checked automatically when we pass an entry on both sides. If both sides of the trial balance are not matched we can easily find the mistake.
- Calculation of Profit or Loss: Profit and Loss Account provides information about the Profit earned or loss incurred during a period.
- Financial Position: The financial position of the business can be determined at the end of the year as we prepare a profit and loss account & Balance Sheet.
- Comparison becomes Easy: We can compare the profit and loss account & Balance Sheet of any two or more years as we have the accounting books.
- Helps a Manager: Manager can take decisions on the basis of the financial condition of the business and make plans accordingly.
- Easily Frauds and Misappropriations: Frauds and misappropriations can be easily found as every transaction has two records.

Disadvantages of Double Entry System

- Complex in nature: Double-entry system is complex in nature as it takes care of lots of rules and regulations of accounting standards & accounting principles.
- Time And Cost: It requires more time to maintain the accounting books so it involves more clerks which leads to an increase in cost.
- Not For Small Firms: Small firms can not hire a person who has proper knowledge of accounting as their charge is high.
- Expert knowledge: It requires expert knowledge of account to use the Double Entry System for book-keeping.
- Increase in book size: Every transaction needs to record in two places so the size of books will increase or those who have data in electronic form need a more powerful computer to handle that data.

Q14.Draw the Performa of Balance sheet and Major involvements

Balance sheet is defined as a statement which sets out the assets and liabilities of a business firm and which serves to as certain the financial position of the same on any particular date. On the left-hand side of this statement, the liabilities and the capital are shown. On the right-hand side all the assets are shown. Therefore, the two sides of the balance sheet should be equal. Otherwise, there is an error somewhere.

BALANCE SHEET OF . . . . AS ON. . . . .

Liabilities	**Amount**	**Assets**	**Amount**
Creditors Bills payable	XXXX	Cash in hand	XXXX
Bank overdraft	XXXX	Cash at bank	XXXX
Loans	XXXX	Bills receivable	XXXX
Mortgage	XXXX	Debtors	XXXX
Reserve fund		Closing stock	XXXX
Capital xxxxxx		Investments	XXXX
Add: Net Profit		Furniture and fittings	XXXX
Less: Drawings	XXXX	Plats&machinery	XXXX
		Land & buildings	XXXX
		Patents, tm ,copyrights Goodwill	XXXX
		Prepaid expenses	XXXX
		Outstanding incomes	XXXX
	XXXX		XXXX

Q15. Explain with examples how you would use ratio analysis to understand financial statements?

Ratio Analysis stands for the process of determining and presenting the relationship of items and groups of items in the financial statements. It is an important technique of financial analysis. It is a way by which financial stability and health of a concern can be judged. The following are the main uses of Ratio analysis:

(i) Useful in financial position analysis: Accounting reveals the financial position of the concern.

This helps banks, insurance companies and other financial institutions in lending and making investment decisions.
(ii) Useful in simplifying accounting figures: Accounting ratios simplify, summaries and systematic the accounting figures in order to make them more understandable and in lucid form.
(iii) Useful in assessing the operational efficiency: Accounting ratios help to have an idea of the working of a concern. The efficiency of the firm becomes evident when analysis is based on accounting ratio. This helps the management to assess financial requirements and the capabilities of various business units.
(iv) Useful in forecasting purposes: If accounting ratios are calculated for a number of years, then a trend is established. This trend helps in setting up future plans and forecasting.
(v) Useful in locating the weak spots of the business: Accounting ratios are of great assistance
in locating the weak spots in the business even though the overall performance may be efficient.
(vi) Useful in comparison of performance: Managers are usually interested to know which department's performance is good and for that they compare one department with the another department of the same firm. Ratios also help him to make any change in the organisation structure.

Q16.Discuss various ratios to analyse the financial statement?

A liquidity ratio is a type of financial ratio used to determine a company's ability to pay its short-term debt obligations. The metric helps determine if a company can use its current, or liquid, assets to cover its current liabilities. There are three types of liquid ratios:

1. Current Ratio

Current Ratio = Current Assets / Current Liabilities

2. Quick Ratio

Quick Ratio = (Cash + Accounts Receivables + Marketable Securities) / Current Liabilities

3. Cash Ratio

Cash Ratio = (Cash + Marketable Securities) / Current Liabilities

Profitability Ratios

This type of ratio helps in measuring the ability of a company in earning sufficient profits.

The types of profitability ratios are: –

Gross Profit Ratios: Gross Profit Ratio = (Gross Profit / Net Sales) * 100

Net Profit Ratio:

Net Profit Ratio = (Net Profit / Net Sales) * 100

Solvency Ratios

Solvency ratios can be defined as a type of ratio that is used to evaluate whether a company is solvent and well capable of paying off its debt obligations or not.

The types of solvency ratios are: –

Debt Equity Ratio: Total Debts / Shareholders Fund

Interest Coverage Ratio: Earnings Before Interest and Taxes / Interest Expense

Turnover Ratios

Turnover ratios are used to determine how efficiently the financial assets and liabilities of an organisation have been used for the purpose of generating revenues.

The types of turnover ratios are: –

Fixed Assets Turnover Ratio = Net Sales / Average Fixed Assets

Inventory Turnover Ratio = Cost of Goods Sold / Average Inventories

Earnings Ratios

Earnings ratio is used for the purpose of determining the returns that an organisation generates for its investors.

The types of earnings ratios are: –

Profit Earnings Ratio = Market Price per Share / Earnings per Share

EPS = (Net Income – Preferred Dividends) / (Weighted Average of Outstanding Shares)

Q17.Outline different types of Liquidity Ratios. Explain different types of Ratios.

Liquidity refers to the ability of an organisation to meet its current obligation. These ratios are used to measure the financial status of an organisation. These ratios help the management to make the decisions about the maintained level of current assets & current libraries of the business. The main purpose to calculate these ratios is to know the short term solvency of the concern. These ratios are

useful to various parties having interest in the enterprise over a short period – such parties include banks. Lenders, suppliers, employees and others.
Current Ratio:

$$CurrentRatio = \frac{CurrentAssets}{CurrentLiablities}$$

Note: The ideal ratio is 2:1 Current Assets = Cash, Bank, Cash Equivalents, Short term Investment, Stock or Inventory, Accounts Receivable, Prepaid Expenses, Receivable Incomes Current Liabilities = Accounts Payable, Notes Payable (Short term Financial Obligations), Bank Overdraft, Current portion of long-term debt, Current Lease payable, Accrued Income, Accrued Expenditure, Dividend Payable, Unearned Revenue, Prereceived Incomes, Outstanding Expenses.
Quick ratio or liquid ratio or acid test ratio: Quick Ratio:

$$CurrentRatio = \frac{QuickAssets}{CurrentLiablities}$$

Note: The ideal ratio is 1:1 Quick assets = cash in hand + cash at bank + short term investments + debtors + bills receivables short term investments are also known as marketable securities.
Super Quick Ratio/ Absolute Liquid Ratio/ Acid Test Ratio:

$$SuperQuickRatio = \frac{SuperQuickAssets}{CurrentLiablities}$$

Note: The ideal ratio is 0:1 or 1:2 Absolute liquid assets=cash in hand + cash at bank + short term investments + marketable securities.

Q18. Differentiate solvency and profitability ratios with examples.

Solvency refers to the ability of a business to honour long item obligations like interest and instalments associated with long term debts. Solvency ratios indicate long term stability of an enterprise. These ratios are used to understand the yield rate of the organisation.
Lenders like financial institutions, debenture, holders, banks are interested in ascertaining solvency of the enterprise. The important solvency ratios are:
Debt Equity Ratio:

$$DebtEquityRatio = \frac{TotalDebt}{Equity} or \frac{OutsidersFunds}{InsidersFunds}$$

Note:The ideal ratio is 2:1 Here, Outsiders funds = Debentures, public deposits, securities, long term bank loans + other long term liabilities. Shareholders funds

= equity share capital + preference share capital + reserves & surpluses + undistributed projects.

Pre Primary Ratio or Equity Ratio:

$$EquityRatio = \frac{TotalEquity}{TotalAssets}$$

The ideal ratio is 1:3 or 0.33:1

Capital Gearing Ratio:

$$CapitalGearingRatio = \frac{Equity, Resurvers\&Surpluses, UndistributedProfit}{OutsidersFunds, PreferenceShareCapital}$$

Debt to Total Fund ratio:

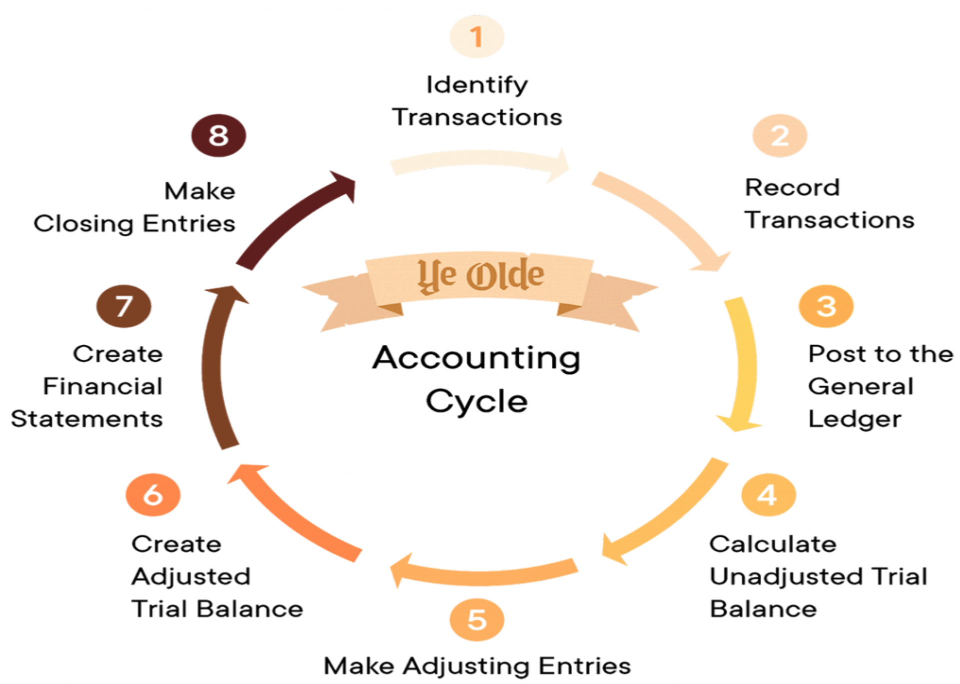
$$DebttoTotalFundRatio = \frac{OutsidersFunds}{CapitalEmployeed}$$

Capital Employed= Outsiders Funds and Shareholders Funds

Shareholders Funds = Debt and Equity

Note:The ideal ratio is 0.67 :1 or 2:3

Q19. Explain the accounting cycle with examples in detail?



Transactions

Transactions: Financial transactions start the process. If there were no financial transactions, there would be nothing to keep track of. Transactions may include a debt payoff, any purchases or acquisition of assets, sales revenue, or any expenses incurred.

Journal Entries

Journal Entries: With the transactions set in place, the next step is to record these entries in the company’s journal in chronological order. In debiting one or more accounts and crediting one or more accounts, the debits and credits must always balance.

Posting to the General Ledger (GL)

Posting to the GL: The journal entries are then posted to the general ledger where a summary of all transactions to individual accounts can be seen.

Trial Balance

Trial Balance: At the end of the accounting period (which may be quarterly, monthly, or yearly, depending on the company), a total balance is calculated for the accounts.

Worksheet

Worksheet: When the debits and credits on the trial balance don’t match, the bookkeeper must look for errors and make corrective adjustments that are tracked on a worksheet.

Adjusting Entries

Adjusting Entries: At the end of the company’s accounting period, adjusting entries must be posted to accounts for accruals and deferrals.

Financial Statements

Financial Statements: The balance sheet, income statement, and cash flow statement can be prepared using the correct balances.

Closing

Closing: The revenue and expense accounts are closed and zeroed out for the next accounting cycle. This is because revenue and expense accounts are income statement accounts, which show performance for a specific period. Balance sheet accounts are not closed because they show the company’s financial position at a certain point in time.

Q20. Classify the difference between capital expenditure and capital receipt.

Difference Between Capital Revenues (Receipt) and Capital Expenditure:

S. No.	Basis for comparison	Capital Revenues	Capital Expenditure
1.	Meaning	Capital revenues are a non-recurring incoming cash flow into the business that leads to the creation of liability and a decrease in company assets.	Capital expenditure is the expenditure that is incurred in acquiring a capital asset or improving the capacity of an existing one, resulting in the extension in its life years.
2.	Effect	Capital revenues effect is long Term.	Its effect is Long Term.
3.	Appears in	We show Capital revenues in the Balance Sheet on the liability side.	We show the Capital expenditures in the Income Statement & Balance Sheet
4.	Nature	These are non-recurring in nature.	These are Non-recurring in nature.
5.	Benefits	Its benefit is enjoyed for many years in the future.	Its benefit is received for more than one year
6.	Increase in value of assets	It decreases the value of asset or we can say that it increases the value of the liability.	It increases the value of assets.
7.	Example	Sale of the fixed asset, loan taken from bank etc.	Cost of land and building, furniture and fixtures etc.

PART C

Q1. Define Financial Accounting.

The purpose of Accounting is to ascertain the financial results i.e. profit or loss in the operations during a specific period. It is also aimed at knowing the financial position, i.e. assets, liabilities and equity position at the end of the period. It also provides other relevant information to the management as a basis for decision-making for planning and controlling the operations of the business.

Q2. Explain the meaning of Journal.

The word Journal is derived from the Latin word 'journ' which means a day. Therefore, a journal means a 'day Book' in which day-to-day business transactions are recorded in chronological order. Journal is treated as the book of original entry or first entry or prime entry. All the business transactions are recorded in this book before they are posted in the ledges. The journal is a complete and chronological (in order of dates) record of business transactions. It is recorded in a systematic manner. The process of recording a transaction in the journal is called "JOURNALISING". The entries made in the book are called "Journal Entries".

The proforma of Journal is given below.

Date	Particulars	LF No	Debit	Credit
1998 Jan 1	Purchases account to cash account (being goods purchased for cash)		10,000/-	10,000/-

Q3. List out different types of Accounting Concepts.

In accountancy following concepts are quite popular.

1.**BUSINESS ENTITY CONCEPT**: In this concept "Business is treated as separate from the proprietor". All the Transactions recorded in the book of Business and not in the books of proprietor. The proprietor is also treated as a creditor for the Business.

2.**GOING CONCERN CONCEPT**: This concept relates with the long life of Business. The assumption is that business will continue to exist for unlimited period unless it is dissolved due to some reasons or the other.

3.**MONEY MEASUREMENT CONCEPT**: In this concept "Only those transactions are recorded in accounting which can be expressed in terms of money, those transactions which can not be expressed in terms of money are not recorded in the books of accounting".

4.**COST CONCEPT**: Accounting to this concept, can asset is recorded at its cost in the books of account. i.e., the price, which is paid at the time of acquiring it. In balance sheet, these assets appear not at cost price every year, but depreciation is deducted and they appear at the amount, which is cost, less classification.

5.**ACCOUNTING PERIOD CONCEPT**: every Businessman wants to know the result of his investment and efforts after a certain period. Usually a one-year period is regarded as an ideal for this purpose. This period is called the Accounting Period. It depends on the nature of the business and object of the proprietor of the business.

6.**DUAL ASPECT CONCEPT**: According to this concept "Every business transaction has two aspects", one is the receiving benefit aspect another one is giving benefit aspect. The receiving benefit aspect is termed as "DEBIT", whereas the giving benefit aspect is termed as "CREDIT". Therefore,for every debit, there will be corresponding credit.

7.**MATCHING COST CONCEPT**: According to this concept "The expenses incurred during an

accounting period, e.g If revenue is recognized on all goods sold during a period, cost of those good sold should also be charged to that period.

8.**REALISATION CONCEPT**: According to this concept revenue is recognized when a sale is made. Sale is Considered to be made at the point when the property in goods posses to the buyer and he becomes legally liable to pay.

Q4.Illustrate the meaning of the Double Entry System.

A double-entry system refers to the system in which the accounts are maintained in a book. All the transactions of a company are maintained in this book.

Double-entry books have two opposite and corresponding entries that are known as credit and debit. The right side is the credit and the left side is the debit. Double-entry meaning also refers to the transactions that are effective in two accounts one that includes debit and the other that includes credit. The accounting equation refers to the detection tool that detects all the errors present in the transactions.

Q5. Recall the meaning of purchase book

This book records all credit purchases only. Purchase of goods for cash and purchase of assets for cash. Credit will not be recorded in this book. Purchases book is otherwise called Purchases Day Book, Purchases Journal or Purchases Register.

Q6. Define subsidiary books

Subsidiary Books are books of Original Entry. They are also known as Day Book or special journals. We record transactions of similar nature are in Subsidiary Books. They are helpful in overcoming the limitations of journal books or journal entries.Subsidiary books are divided into eight types. They are:-

1. Purchases Book
2. Sales Book
3. Purchase Returns Book
4. Sales Returns Book
5. Cash Book
6. Bills Receivable Book
7. Bills Payable Book
8. Journal Proper

Q7. Explain the meaning of trial balance.

A trial balance is a bookkeeping worksheet in which the balance of all ledgers are compiled into debit and credit account column totals that are equal. A company prepares a trial balance periodically, usually at the end of every reporting period.

The general purpose of producing a trial balance is to ensure the entries in a company's bookkeeping system are mathematically correct.

Q8. List out the errors of principle

An error of principle is an accounting mistake in which an entry violates a fundamental principle of accounting or a fundamental accounting principle established by a company.

Q9. Outline few lines of Errors of Omission

When some transactions are completely omitted from the books of accounts or entered but not posted, they are treated as errors of omission.

If a transaction is omitted altogether from the books of **accounts**, there would be neither a **debit** nor a **credit** entry in the ledger. Hence, the **trial balance** will not be affected.

The types of Errors of Omission are:-

- Partial Omission
- Complete Omission

Q10. Write a note on provisions for doubtful debts.

The provision for doubtful debts is the estimated amount of bad debt that will arise from accounts receivable that have been issued but not yet collected. It is identical to the allowance for doubtful accounts. The provision is used under accrual basis accounting, so that an expense is recognized for probable bad debts as soon as invoices are issued to customers, rather than waiting several months to find out exactly which invoices turned out to be uncollectible.

Q11. Explain the Meaning of Revenue Receipt

Revenue receipts can be defined as those receipts which neither create any liability nor cause any reduction in the assets of the government. They are regular and recurring in nature and the government receives them in the normal course of activities.Revenue receipts include the proceeds from taxes and other duties levied by the Centre; the interest and dividend it receives on its investments; and the fees and charges the government receives for its services.

Simply put, revenue receipts must satisfy two basic conditions:

No liability: Revenue receipts do not create any liability for the government. For example, taxes received by the government, unlike borrowings, do not create any liabilities for it.

No asset reduction: Revenue receipts do not lead to any reduction in the government's assets. So, the government cannot show its earnings from sale of stake in a public-sector undertaking as revenue receipts because the stake sale resulted in reduction of its assets.

Q12. Write the meaning of Contra Entry.

Contra entry refers to transactions involving cash and bank accounts. In other words, any entry which affects both cash and bank accounts is called a contra entry. Contra in Latin means the opposite. It is more popularly known as contra voucher.

To make the definition further simpler, any transactions involving a transfer of cash between one cash a/c to another or one cash a/c to another bank a/c or one bank account to another is called a contra entry.

Q13. Illustrate the meaning of a ledger account.

An accounting ledger is an account or record used to store bookkeeping entries for balance-sheet and income-statement transactions. Accounting ledger journal entries can include accounts like cash, accounts receivable, investments, inventory, accounts payable, accrued expenses, and customer deposits. Accounting ledgers are maintained for all types of balance sheet and income statement transactions.

The accounting ledger is used to generate the key financial statements: the income statement, cash flow statement, and balance sheet for the company. "Posting" to an accounting ledger is the bookkeeping process of recording credits and debits. You can think of the accounting ledger as a collection of the chart of accounts, which is where all accounting journal entries end up.

Q14. Illustrate the meaning of Capital Expenditure.

Capital expenditures refer to funds that are used by a company for the purchase, improvement, or maintenance of long-term assets to improve the efficiency or capacity of the company. Long-term assets are usually physical, fixed and non-consumable assets such as property, equipment, or infrastructure, and that have a useful life of more than one accounting period.

Also known as CapEx or capital expenses, capital expenditures include the purchase of items such as new equipment, machinery, land, plant, buildings or warehouses, furniture and fixtures, business vehicles, software, or intangible assets such as a patent or license.

Q15. List out different types of Accounting Conventions.

Accounting is based on some customs or usages. Naturally accountants here adopt that usage or custom. They are termed as convert conventions in accounting. The following are some of the important accounting conventions.

1.FULL DISCLOSURE: According to this convention accounting reports should disclose fully and fairly the information. They purport to represent. They should be prepared honestly and sufficiently disclose information which is of material interest to proprietors, present and potential creditors and investors. The companies ACT, 1956 makes it compulsory to provide all the information in the prescribed form.

2.MATERIALITY: Under this convention the trader records important factors about the commercial activities. In the form of financial statements if any unimportant information is to be given for the sake of clarity it will be given as footnotes.

3.CONSISTENCY: It means that the accounting method adopted should not be changed from year to year. It means that there should be consistent in the methods or principles followed. Or else the results of a year cannot be conveniently compared with that of another.

4. CONSERVATISM: This convention warns the trader not to take unrealized income into account. That is why the practice of valuing stock at cost or market price, whichever is lower, is vague. This is the policy of "playing safe"; it takes in to consideration all prospective losses but leaves all prospective profits.

Q16. Write a short note on Current ratio?

The current ratio is a liquidity ratio that measures a company's ability to pay short-term obligations or those due within one year. It tells investors and analysts how a company can maximize the current assets on its balance sheet to satisfy its current debt and other payables.

Note: The ideal ratio is 2:1 Current Assets = Cash, Bank, Cash Equivalents, Short term Investment, Stock or Inventory, Accounts Receivable, Prepaid Expenses, Receivable Incomes Current Liabilities = Accounts Payable, Notes Payable (Short term Financial Obligations), Bank Overdraft, Current portion of long-term debt, Current Lease payable, Accrued Income, Accrued Expenditure, Dividend Payable, Unearned Revenue, Prereceived Incomes, Outstanding Expenses.

$$CurrentRatio = \frac{CurrentAssets}{CurrentLiablities}$$

Q17. Illustrate the formula for Operating ratio.

The operating ratio formula is the ratio of the company's operating expenses to net sales. Operating expenses include administrative expenses, selling and distribution expenses, cost of goods sold,salary, rent, other labor costs, depreciation etc.

$$OperatingRatio = \frac{OperatingExpenses}{NetSales} \times 100$$

Q18. Define the formula for Debt Equity Ratio?

The debt-equity ratio is a measure of the relative contribution of the creditors and shareholders or owners in the capital employed in business.

$$DebtEquityRatio = \frac{TotalDebt}{Equity} or \frac{OutsidersFunds}{InsidersFunds}$$

Note:The ideal ratio is 2:1 Here, Outsiders funds = Debentures, public deposits, securities, long term bank loans + other long term liabilities. Shareholders funds = equity share capital + preference share capital + reserves & surpluses + undistributed projects.

Q19. List out the limitations of ratio analysis.

These limitations should be kept in mind while making use of ratio analyses for interpreting the financial statements. The following are the main limitations of ratio analysis.

1. False results if based on incorrect accounting data

2. No idea of probable happenings in future

3. Variation in accounting methods

4. Price level change

5. Only one method of analysis

6. No common standards

7. Different meanings assigned to the some term

8. Ignores qualitative factors

9. No use if ratios are worked out for insignificant and unrelated figure

Q20. What is the meaning of Return on Capital Employed?

Return on capital employed (ROCE) is a financial ratio that can be used to assess a company's profitability and capital efficiency. In other words, this ratio can help to understand how well a company is generating profits from its capital as it is put to use.

The ROCE ratio is one of several profitability ratios financial managers, stakeholders, and potential investors may use when analysing a company for investment.