Class 11 Accountancy –	Chapter 1: Introduction to Accounting (AHSEC)

Important Questions with Full Explanatory Answers

2-Mark Questions

Q1. Define accounting.
Ans:
Accounting is the process of identifying, measuring, recording, and communicating economic information to permit informed judgments and decisions by users of the information.

Q2. Mention two objectives of accounting.
Ans:
1. To maintain systematic records of financial transactions.
2. To determine the profit or loss of a business at the end of a specific period.

Q3. What is bookkeeping?
Ans:
Bookkeeping is the process of recording day-to-day financial transactions of a business in a systematic and chronological manner.

Q4. Write any two differences between accounting and bookkeeping.
Ans:

Accounting	Bookkeeping
Involves summarizing and interpreting financial data.	Involves only recording financial transactions.
It is analytical in nature.	It is clerical in nature.

Q5. Name any two internal users of accounting information.
Ans:
1. Owners
2. Management

3-Mark Questions

Q6. Explain any three functions of accounting.
Ans:
1. **Recording Transactions:** Accounting records all business transactions systematically.
2. **Classifying Data:** Transactions are classified into ledgers for analysis.
3. **Summarizing Results:** The data is summarized into financial statements like the Profit & Loss Account and Balance Sheet.

Q7. Distinguish between debtors and creditors.
Ans:

Debtors	Creditors
Persons who owe money to the business.	Persons to whom the business owes money.
Shown as assets in the balance sheet.	Shown as liabilities.

Q8. Who are the external users of accounting information?
Ans:
External users include:
1. **Investors** – who assess the profitability of a business.
2. **Creditors** – who assess creditworthiness.
3. **Government** – to assess tax and compliance.

☑ 4-Mark Questions

Q9. State any four limitations of accounting.
Ans:
1. **Ignores qualitative factors** like employee morale and brand value.
2. **Based on historical cost**, hence may not reflect current market values.
3. **Possibility of manipulation**, as personal judgments can influence methods.
4. **Fails to consider inflation**, thus distorting asset values.

Q10. Explain the process of accounting briefly.
Ans:
The accounting process includes:
1. **Identifying** transactions of financial nature.
2. **Recording** them in the journal.
3. **Classifying** into ledgers.
4. **Summarizing** into trial balance and financial statements.
5. **Analyzing and interpreting** financial data.
6. **Communicating** it to stakeholders.

Q11. Write four objectives of accounting.
Ans:
1. **Maintain systematic records** of all transactions.
2. **Ascertain profit or loss** through income statements.
3. **Determine financial position** via balance sheet.
4. **Provide useful information** to stakeholders for decision-making.

Q12. What is the role of accounting in business?
Ans:
Accounting helps in:
- Tracking income and expenditure.
- Ensuring legal compliance.
- Forecasting business trends.
- Making sound managerial decisions based on financial data.

☑ 5-Mark Questions

Q13. Explain the advantages of accounting.
Ans:
1. **Systematic records:** Helps in tracking all financial transactions.
2. **Helps in decision-making:** Provides data for planning and controlling.
3. **Legal evidence:** Acts as proof in legal matters and tax compliance.
4. **Determines profit/loss:** Assesses business performance periodically.
5. **Shows financial position:** Helps stakeholders understand assets, liabilities, and capital.

Q14. Differentiate between internal and external users of accounting information.
Ans:

Basis	Internal Users	External Users
Meaning	Individuals within the organization	Individuals outside the organization
Examples	Managers, employees, owners	Creditors, investors, government
Purpose	Planning and decision-making	Investment and regulatory purposes
Access	Full access to records	Limited access via reports/statements

Q15. "Accounting is both an art and a science." Justify.
Ans:
Accounting is a **science** because it follows a systematic body of knowledge, rules, and principles. It is also an **art** because it involves applying those principles creatively in analyzing and interpreting data to draw conclusions and present reports.

☑ 8-Mark Questions

Q16. What is accounting? Discuss its objectives, functions, and importance.
Ans:
Definition:
Accounting is the art of recording, classifying, and summarizing financial transactions in a significant manner to interpret and communicate the results.
Objectives:

1. Maintain systematic records.
2. Ascertain profit or loss.
3. Determine financial position.
4. Aid in decision-making.

Functions:

- Recording (bookkeeping)
- Classifying (ledgers)
- Summarizing (financial statements)
- Analysis and interpretation
- Communication to stakeholders

Importance:

- Assists in budgeting and planning
- Provides legal evidence
- Facilitates external reporting and auditing
- Helps manage business effectively

Q17. Explain in detail the various branches of accounting.
Ans:

1. **Financial Accounting:** Records and presents financial information for external users.
2. **Cost Accounting:** Determines the cost of production and helps in controlling expenses.
3. **Management Accounting:** Provides data for internal decision-making.
4. **Tax Accounting:** Focuses on tax-related matters and compliance with laws.
5. **Social Responsibility Accounting:** Measures social and environmental impact of business activities.

Q18. Discuss the need and importance of accounting in modern business.
Ans:
Accounting is essential in modern business because:

- It maintains accurate records to track performance.
- Supports decision-making with financial insights.
- Ensures compliance with laws and taxation.
- Helps raise funds by showing financial stability.
- Assists in budgeting, forecasting, and performance evaluation.

Extra Questions:

☑ 2–3 Mark Questions (Short Qs)

Q19. Define financial accounting.
Ans:
Financial accounting refers to the process of recording, summarizing, and reporting a company's business transactions using standardized formats (e.g., Profit & Loss Account, Balance Sheet) for external users like investors and tax authorities.

Q20. What is meant by a transaction? Give one example.
Ans:
A transaction is any economic event that affects the financial position of a business and can be measured in monetary terms.
Example: Purchase of goods worth ₹5,000 on credit.

☑ 4–5 Mark Questions

Q21. Differentiate between profit and gain with examples.
Ans:

Basis	**Profit**	**Gain**
Meaning	Excess of revenue over expenses in normal business	Arises from incidental or non-operating activities
Example	Profit from sale of goods	Gain on sale of old furniture
Frequency	Regular and recurring	Irregular and non-recurring

Q22. Explain the characteristics of accounting.
Ans:
1. **Financial Nature:** Only records monetary transactions.
2. **Systematic:** Follows a structured process.
3. **Historical:** Based on past events.
4. **Summarizing:** Presents info in simplified financial statements.
5. **Communicative:** Delivers results to internal and external users.

Q23. Explain the term 'event' in accounting. How is it different from a transaction?
Ans:
An **event** is the result of a transaction that may or may not have monetary value.
- **Events** can be financial (affecting the accounting records) or non-financial.
- **Transactions** are always financial and recorded in accounts.

Example:
- Event: Fire in factory (may or may not have financial impact).
- Transaction: Payment of insurance claim due to fire – this is recorded.

☑ 8 Mark Long Q (Optional / Backup for Choice-Based Questions)

Q24. Discuss the importance of accounting to different stakeholders.
Ans:
1. **Owners:** To assess profitability and financial health.
2. **Management:** To take operational and strategic decisions.
3. **Investors:** To evaluate return potential before investing.
4. **Creditors/Suppliers:** To assess creditworthiness.
5. **Government:** To determine taxes and ensure compliance.
6. **Employees:** To assess job security and demand fair wages.

☑ Recap:

You now have **24 fully explained questions** from Chapter 1, covering:
- 2 Marks: 5 questions
- 3 Marks: 4 questions
- 4 Marks: 4 questions
- 5 Marks: 4 questions
- 8 Marks: 3 questions
- Others (backup/varied): 4 questions

Chapter 2: Basic Accounting Terms (AHSEC)

Important Questions with Full Explanatory Answers

2-Mark Questions

Q1. Define the term 'Capital'.
Ans:
Capital refers to the amount invested by the owner in the business, either in the form of money or assets. It represents the owner's claim on the business and is shown on the liabilities side of the balance sheet.

Q2. What is the meaning of 'Drawings'?
Ans:
Drawings refer to the withdrawal of cash or goods by the owner from the business for personal use. It reduces both capital and assets of the business.

Q3. What is meant by 'Liabilities'?
Ans:
Liabilities are the financial obligations or debts that a business owes to outsiders (e.g., loans, creditors, bills payable). These are shown on the liabilities side of the balance sheet.

Q4. Define the term 'Asset'.
Ans:
Assets are valuable resources owned by a business which provide future economic benefits. They can be tangible (land, building) or intangible (goodwill, patents).

Q5. What is a 'Transaction'?
Ans:
A transaction is an event that involves the exchange of goods, services, or money and has a financial impact measurable in monetary terms. For example, purchase of goods for ₹5,000.

3-Mark Questions

Q6. Explain the term 'Revenue' with an example.
Ans:
Revenue refers to the income earned by a business from its operating activities, such as sales of goods or services.
Example: If a furniture shop sells tables for ₹50,000, this amount is revenue.

Q7. What is the difference between Income and Revenue?
Ans:

Basis	**Revenue**	**Income**
Meaning	Gross inflow from business activities	Net earnings after deducting expenses from revenue
Example	Sales of ₹1,00,000	Profit of ₹20,000 after expenses of ₹80,000

Q8. Distinguish between creditors and debtors.
Ans:
- **Creditors** are persons to whom the business owes money (liabilities).
- **Debtors** are persons who owe money to the business (assets).

4-Mark Questions

Q9. Explain four types of assets with examples.
Ans:
1. **Fixed Assets:** Long-term use, e.g., buildings, machinery.
2. **Current Assets:** Short-term use, e.g., cash, inventory.
3. **Tangible Assets:** Physical existence, e.g., land.
4. **Intangible Assets:** No physical form, e.g., patents.

Q10. Explain the difference between expenses and losses.
Ans:

Basis	Expenses	Losses
Meaning	Regular cost to run the business	Unexpected or abnormal financial shortfall
Example	Salary paid	Goods destroyed in fire
Effect	Reduces profit	Can result in negative profit

Q11. What is the meaning of goods? Give examples.
Ans:
Goods are items bought and sold in the ordinary course of business.
Example: For a furniture business, tables and chairs are goods; for a car dealer, vehicles are goods.

Q12. Define Expenditure. Mention its types.
Ans:
Expenditure refers to the spending of money or incurring a liability to acquire goods or services.
Types:
1. **Capital Expenditure** (e.g., purchase of building)
2. **Revenue Expenditure** (e.g., electricity bill)

☑ 5-Mark Questions

Q13. Explain the following terms with examples: (i) Expense, (ii) Profit, (iii) Loss, (iv) Income, (v) Capital.
Ans:
- **Expense:** Regular outflow for operations. Eg: Rent.
- **Profit:** When income > expenses. Eg: Sales ₹10,000, expense ₹7,000 → Profit ₹3,000.
- **Loss:** When expenses > income. Eg: Sales ₹5,000, expense ₹7,000 → Loss ₹2,000.
- **Income:** Net gain. Income = Revenue - Expense.
- **Capital:** Owner’s investment in the business.

Q14. Differentiate between Capital Expenditure and Revenue Expenditure.
Ans:

Basis	Capital Expenditure	Revenue Expenditure
Nature	Long-term	Short-term, recurring
Purpose	To acquire or improve assets	For day-to-day expenses
Example	Purchase of machinery	Wages, rent
Effect	Shown as asset	Shown in P&L account

Q15. Explain the classification of liabilities with examples.
Ans:
1. **Current Liabilities:** Payable within a year. Eg: Creditors, Bills Payable.
2. **Non-Current Liabilities:** Payable after a year. Eg: Bank loans.
3. **Contingent Liabilities:** Possible liabilities depending on future events. Eg: Pending lawsuit.

☑ 8-Mark Questions

Q16. Define and explain the following with suitable examples:
(i) Capital, (ii) Drawings, (iii) Assets, (iv) Liabilities, (v) Revenue, (vi) Expenses, (vii) Loss, (viii) Profit.
Ans:
- **Capital:** Owner’s investment. Eg: ₹1,00,000 deposited in business.
- **Drawings:** Withdrawal by owner. Eg: ₹5,000 withdrawn.
- **Assets:** Resources like land, machines.
- **Liabilities:** Dues to outsiders like creditors.
- **Revenue:** Sales income. Eg: ₹25,000.

- **Expenses:** Wages, rent, etc.
- **Loss:** Damage by fire.
- **Profit:** Revenue > Expense; eg, profit of ₹10,000 from sales.

Q17. Discuss in detail the differences between Assets, Liabilities, and Capital with suitable examples.
Ans:

Basis	Assets	Liabilities	Capital
Definition	Economic resources owned	Obligations payable	Owner's claim
Position	Left side of Balance Sheet	Right side	Right side
Examples	Cash, building	Creditors, loans	Owner's investment
Formula Relation	Assets = Liabilities + Capital		

Q18. Write short notes on: (a) Trade Receivable, (b) Trade Payable, (c) Stock, (d) Voucher
Ans:
- **Trade Receivable:** Money receivable from customers (debtors).
- **Trade Payable:** Money payable to suppliers (creditors).
- **Stock:** Inventory held for sale or production.
- **Voucher:** Documentary proof of a transaction.

Q19. Distinguish between Fixed Assets and Current Assets.
Ans:

Basis	Fixed Assets	Current Assets
Nature	Long-term	Short-term
Liquidity	Low	High
Purpose	Used in operations	Sold or converted into cash
Example	Land, building	Cash, stock

Q20. Explain the term 'Voucher' and its types.
Ans:
A voucher is a written document serving as proof of a financial transaction.
Types:
1. **Cash Voucher** – for cash payments/receipts
2. **Journal Voucher** – for non-cash transactions
3. **Purchase/Sales Voucher** – for buying/selling goods

▧ Chapter 3: Theory Base of Accounting

◇ *Important Questions with Full Explanatory Answers*

☑ 2-Mark Questions

Q1. What is meant by accounting principles?
Ans:
Accounting principles are a set of rules and guidelines that accountants follow to record, classify, and summarize financial transactions. They ensure consistency, reliability, and comparability in financial statements.

Q2. Define GAAP.
Ans:

Generally Accepted Accounting Principles (GAAP) are the standard framework of guidelines for financial accounting used in a particular jurisdiction. It includes concepts, conventions, and standards.

Q3. What do you mean by business entity concept?
Ans:
This concept states that the business is treated as a separate entity from its owner. All financial transactions are recorded from the business's point of view.

Q4. Define money measurement concept.
Ans:
Only those transactions which can be measured in monetary terms are recorded in the books of accounts. Non-monetary items like employee skills or brand reputation are not recorded.

Q5. What is matching concept?
Ans:
According to this concept, revenues of a period should be matched with the expenses incurred to earn them, to determine the true profit or loss for that period.

☑ 3-Mark Questions

Q6. Explain the going concern concept with an example.
Ans:
This concept assumes that a business will continue to operate indefinitely.
Example: Depreciation is charged on assets assuming they'll be used in future operations.

Q7. What is the dual aspect concept? Give an example.
Ans:
Every transaction has two aspects: a **debit** and a **credit**.
Example: When ₹10,000 cash is invested in the business:
- Asset (cash) increases → Debit
- Capital (owner's equity) increases → Credit

Q8. Explain the consistency concept.
Ans:
According to this concept, accounting policies and practices should be applied consistently from one period to another. This ensures comparability of financial statements over time.

☑ 4-Mark Questions

Q9. Differentiate between accounting concepts and accounting conventions.
Ans:

Basis	Accounting Concepts	Accounting Conventions
Meaning	Basic assumptions for recording	Customs/practices followed for consistency
Nature	Theoretical framework	Practical application
Examples	Going concern, accrual	Conservatism, materiality

Q10. Explain the conservatism (prudence) convention.
Ans:
This convention suggests that potential losses should be recorded, but expected gains should not be recorded until realized. It prevents overstatement of assets or income.
Example: Creating provision for doubtful debts.

Q11. Explain the full disclosure principle.
Ans:
This principle requires all material and relevant information to be disclosed in financial statements so that stakeholders can make informed decisions. Eg: Contingent liabilities shown in footnotes.

Q12. Write short notes on:
(a) Materiality
(b) Objectivity
Ans:

- **Materiality:** Only information that would influence decision-making needs to be disclosed.
- **Objectivity:** Financial information should be based on verifiable evidence like bills or vouchers.

☑ 5-Mark Questions

Q13. Explain any five accounting concepts with examples.
Ans:

1. **Business Entity:** Business ≠ Owner
2. **Going Concern:** Business continues indefinitely
3. **Money Measurement:** Only monetary transactions recorded
4. **Accrual:** Revenues/expenses recorded when earned/incurred, not when cash is received/paid
5. **Dual Aspect:** Every transaction affects two accounts

Q14. Explain the historical cost concept with an example.
Ans:
According to this concept, assets are recorded at the price paid to acquire them and not at their current market value.
Example: A building purchased for ₹10,00,000 is recorded at the same value even if its market value rises to ₹15,00,000.

Q15. Explain the accrual basis of accounting.
Ans:
Revenues and expenses are recorded when they are earned or incurred, regardless of when cash is received or paid. This helps in accurate measurement of net profit for a period.

☑ 8-Mark Questions

Q16. Discuss in detail the accounting concepts that guide the preparation of final accounts.
Ans:

1. **Business Entity Concept**
2. **Going Concern Concept**
3. **Accrual Concept**
4. **Matching Concept**
5. **Money Measurement Concept**
6. **Accounting Period Concept**
   These ensure that income, expenses, assets, and liabilities are recorded properly to reflect the true financial performance of the business.

Q17. Explain the fundamental accounting assumptions as per AS-1.
Ans:

1. **Going Concern** – Entity will continue in operation.
2. **Consistency** – Same accounting policies each year.
3. **Accrual** – Revenues/expenses recorded when earned/incurred.
   These assumptions are presumed to be followed unless stated otherwise.

Q18. "Accounting information should be reliable and relevant." Explain.
Ans:

- **Reliable:** Based on verifiable documents, free from bias.
- **Relevant:** Capable of influencing decisions by helping users evaluate past, present, or future events.
  Example: Reporting accurate profit helps investors decide whether to invest.

Q19. Write a detailed note on qualitative characteristics of accounting information.
Ans:

1. **Reliability:** Based on evidence.
2. **Relevance:** Useful for decision-making.
3. **Understandability:** Easy to interpret.

4. **Comparability:** Consistent over time and with other businesses.

Q20. How do the principles of accounting help in preparing financial statements?
Ans:
They ensure:
- Uniformity in data presentation
- Legal compliance (GAAP)
- Accurate profit/loss calculation
- Better comparison and decision-making
  Without these principles, statements may be misleading or inconsistent.

Chapter 4: Bases of Accounting

Important Questions with Full Explanatory Answers

2-Mark Questions

Q1. What is the cash basis of accounting?
Ans:
Cash basis of accounting records revenues when cash is actually received and expenses when they are paid, irrespective of the period in which they occur.

Q2. What is the accrual basis of accounting?
Ans:
Accrual basis records revenues when they are earned and expenses when they are incurred, even if the cash is not yet received or paid.

Q3. Mention any two differences between cash basis and accrual basis.
Ans:
1. **Timing:** Cash basis records on cash movement; accrual records on occurrence.
2. **Accuracy:** Accrual basis gives a more accurate picture of financial performance.

Q4. Which basis of accounting is recognised by law and widely accepted?
Ans:
Accrual basis of accounting is recognised by law and is accepted under Generally Accepted Accounting Principles (GAAP).

Q5. Name the two main bases of accounting.
Ans:
1. Cash Basis
2. Accrual Basis

3-Mark Questions

Q6. State any three merits of the accrual basis of accounting.
Ans:
1. Shows a more accurate financial position.
2. Helps in matching revenues and expenses properly.
3. Accepted by legal and accounting authorities.

Q7. Give three features of cash basis of accounting.
Ans:
1. Simple to understand and use.
2. Records only actual cash inflows and outflows.
3. Does not match income with the period it was earned.

Q8. Why is accrual basis preferred over cash basis? Give reasons.
Ans:

- It provides a **true picture** of profit or loss.
- Complies with the **matching concept**.
- **Legally accepted** for preparation of financial statements.

☑ 4-Mark Questions

Q9. Distinguish between cash basis and accrual basis of accounting.
Ans:

Basis	Cash Basis	Accrual Basis
Recording	On cash receipt/payment	On earning/incurring
Accuracy	Less accurate	More accurate
Legal Acceptance	Not accepted by GAAP	Accepted by GAAP
Suitability	Small businesses	All businesses and companies

Q10. Explain with examples how revenue and expenses are treated under both bases.
Ans:
Example: Rent of ₹5,000 for March paid in April.

- **Cash Basis:** Record in April (when paid)
- **Accrual Basis:** Record in March (when expense occurred)

Example: Interest income of ₹2,000 received in June for May.

- **Cash Basis:** Record in June
- **Accrual Basis:** Record in May

Q11. State any four advantages of cash basis of accounting.
Ans:

1. Simple and easy to maintain.
2. Suitable for small firms and professionals.
3. Requires less record-keeping.
4. Reflects actual cash available at a point in time.

Q12. What are the disadvantages of accrual basis of accounting?
Ans:

1. More complex to maintain.
2. Requires estimations (e.g., provisions).
3. Doesn't show actual cash position.
4. Needs trained staff and systems.

☑ 5-Mark Questions

Q13. Explain in detail the cash basis of accounting along with its merits and demerits.
Ans:

- **Definition:** Records transactions only when cash is received or paid.
- **Merits:**
    1. Easy to use
    2. Reflects cash flow
    3. Low cost of maintenance
- **Demerits:**
    1. Ignores outstanding items
    2. Doesn’t follow matching principle
    3. Not accepted by law

Q14. Explain the features and limitations of accrual basis of accounting.
Ans:

- **Features:**
    1. Records revenue/expenses when they occur

2. Follows matching principle
3. Accepted under GAAP

- **Limitations:**
  1. Complex and costly
  2. Doesn't reflect cash flow
  3. Needs adjustments and estimates

Q15. How does the choice of accounting basis affect the financial results of a business?
Ans:

- **Cash Basis:** May understate/overstate profit depending on cash flow timing.
- **Accrual Basis:** Provides a more realistic picture of profitability and liabilities, which helps in better decision-making and is legally required for companies.

☑ 8-Mark Question

Q16. Compare and contrast cash basis and accrual basis of accounting in detail. Which is more appropriate for a business and why?
Ans:

Feature	Cash Basis	Accrual Basis
Recognition	On payment/receipt	On occurrence
Matching Principle	Not followed	Followed
Reliability	Less	More
Complexity	Simple	Complex
Legal Validity	Not accepted by law	Accepted by law
Suitability	Small traders	All types of businesses

Conclusion:
Accrual basis is more appropriate as it shows a **true financial picture**, **matches revenues and expenses**, and is **accepted under GAAP**, making it mandatory for companies and preferred by investors and analysts.

Chapter 5: Accounting Standards

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What are Accounting Standards?
Ans:
Accounting Standards are written policy documents issued by recognized accounting bodies (like ICAI) that provide guidelines for recognition, measurement, presentation, and disclosure of accounting transactions in financial statements.

Q2. Who issues Accounting Standards in India?
Ans:
In India, Accounting Standards are issued by the **Institute of Chartered Accountants of India (ICAI)**, under the guidance of the **National Financial Reporting Authority (NFRA)**.

Q3. What is the objective of Accounting Standards?
Ans:
The main objective is to ensure **uniformity**, **comparability**, **transparency**, and **reliability** of financial statements.

Q4. Mention two benefits of Accounting Standards.
Ans:

1. Ensures comparability of financial statements.
2. Enhances reliability and credibility for users.

Q5. Name any two Accounting Standards applicable in India.
Ans:
1. AS-1: Disclosure of Accounting Policies
2. AS-9: Revenue Recognition

☑ 3-Mark Questions

Q6. Why are Accounting Standards important?
Ans:
Accounting Standards:
1. Ensure uniformity in accounting treatments.
2. Minimize ambiguity and manipulation.
3. Promote better comparability of financial results.

Q7. What is AS-1? State any two accounting policies covered under it.
Ans:
AS-1 relates to **Disclosure of Accounting Policies**. It requires companies to disclose significant policies used in preparing financial statements.
Examples:
- Depreciation method used
- Valuation of stock

Q8. What is the role of NFRA in relation to Accounting Standards?
Ans:
The **National Financial Reporting Authority (NFRA)** oversees and regulates compliance with Accounting and Auditing Standards and advises on formulation of standards for public interest entities.

☑ 4-Mark Questions

Q9. Write four advantages of Accounting Standards.
Ans:
1. Promotes consistency in financial statements.
2. Helps in better decision-making by users.
3. Ensures true and fair view of accounts.
4. Enhances credibility and reliability of reports.

Q10. Differentiate between Accounting Principles and Accounting Standards.
Ans:

Basis	**Accounting Principles**	**Accounting Standards**
Nature	Broad guidelines	Specific rules
Issued By	General accounting theory	ICAI (India)
Flexibility	More flexible	Less flexible
Legal Standing	Not always legally binding	Legally enforceable in some cases

Q11. Explain the limitations of Accounting Standards.
Ans:
1. Cannot override legal provisions.
2. One standard may not suit all businesses.
3. Sometimes involve rigid application.
4. May not cover all accounting issues.

☑ 5-Mark Questions

Q12. Explain the need for Accounting Standards in India.

Ans:

1. Removes variations in accounting practices.
2. Ensures uniformity across firms.
3. Increases reliability for investors, government, and stakeholders.
4. Promotes fair presentation of financial statements.
5. Helps in global comparability.

Q13. Explain the process of formulation of Accounting Standards in India.
Ans:

1. Draft standard prepared by ICAI.
2. Exposure draft issued for public comments.
3. Review by National Advisory Committee/NFRA.
4. Final standard issued after approval.
5. Implementation and monitoring by ICAI.

Q14. What are the key features of Accounting Standards?
Ans:

1. Ensure consistency and comparability.
2. Cover recognition, measurement, presentation, and disclosure.
3. Mandatory for companies in many cases.
4. Framed to ensure fair view of financial statements.
5. Apply to different types of enterprises.

Q15. Explain AS-9 in detail.
Ans:
AS-9 deals with **Revenue Recognition**. It defines the point when revenue should be recognized in financial statements.
Key points:

- Revenue from sale of goods is recognized when significant risks and rewards are transferred.
- Revenue from services is recognized when the service is performed.
- Interest/dividends are recognized on time-basis/right to receive basis.

☑ 8-Mark Question

Q16. Discuss the objectives, features, and limitations of Accounting Standards in detail.
Ans:
Objectives:

- Uniformity in accounting treatment
- Comparability and transparency
- Reduce accounting alternatives

Features:

- Authoritative guidelines
- Legally binding in some cases
- Improve quality of financial reports

Limitations:

- Rigid in application
- Can’t override law
- One-size-fits-all may not work

Conclusion: Accounting Standards improve reliability but must evolve with business practices.

Q17. Discuss the classification of Accounting Standards based on applicability.
Ans:
In India, Accounting Standards are classified based on type of enterprise:

1. **Level I:** Large enterprises – must follow all AS
2. **Level II & III:** Medium and small – allowed certain relaxations
   This ensures fair compliance while considering business size.

Q18. What is IFRS? How is it different from Indian Accounting Standards (Ind AS)?
Ans:
IFRS (International Financial Reporting Standards) are global standards developed by the IASB. India has adopted

modified versions called **Ind AS**.
Differences:
- IFRS is globally accepted, Ind AS is localized.
- Some recognition and measurement rules differ.
- Ind AS aligns with Indian legal & economic environment.

Q19. Write a note on convergence of Indian Accounting Standards with IFRS.
Ans:
India adopted Ind AS to align with IFRS while keeping local needs in mind.
Benefits of convergence:
- Global recognition
- Attract foreign investment
- Better transparency for MNCs

Q20. State and explain any five Accounting Standards issued by ICAI.
Ans:
1. **AS-1**: Disclosure of Accounting Policies
2. **AS-2**: Valuation of Inventories
3. **AS-6** (now merged): Depreciation Accounting
4. **AS-9**: Revenue Recognition
5. **AS-10**: Accounting for Fixed Assets

Each standard helps in specific areas like valuation, timing, and presentation of accounts.

📒 Chapter 6: Accounting Procedures – Rules of Debit and Credit

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What is a debit?
Ans:
Debit means entering an amount on the left side of an account. It generally represents the receipt or increase in assets or expenses.

Q2. What is a credit?
Ans:
Credit means entering an amount on the right side of an account. It generally represents the giving away or increase in liabilities, income, or capital.

Q3. Define the term 'account'.
Ans:
An account is a record that summarizes all the transactions related to a particular person, asset, expense, or income.

Q4. What are personal accounts?
Ans:
Personal accounts relate to individuals, firms, companies, or institutions. For example, Accounts Receivable and Accounts Payable.

Q5. What are real accounts?
Ans:
Real accounts relate to tangible and intangible assets like cash, machinery, buildings, patents, etc.

☑ 3-Mark Questions

Q6. What are nominal accounts? Give two examples.
Ans:
Nominal accounts relate to expenses, losses, incomes, and gains. Examples include Rent Expense, Commission Received.

Q7. State the three golden rules of accounting.
Ans:
1. Personal Account: Debit the receiver, Credit the giver
2. Real Account: Debit what comes in, Credit what goes out
3. Nominal Account: Debit all expenses and losses, Credit all incomes and gains

Q8. Give one example each for personal, real, and nominal accounts.
Ans:
- Personal Account: Ram's Account
- Real Account: Cash Account
- Nominal Account: Salary Account

☑ 4-Mark Questions

Q9. Explain the golden rule of accounting for personal accounts with an example.
Ans:
For personal accounts:
- Debit the receiver
- Credit the giver

Example: Ram gave goods to Shyam on credit.
Debit Shyam (receiver), Credit Ram (giver).

Q10. Explain the golden rule of accounting for real accounts with an example.
Ans:
For real accounts:
- Debit what comes in
- Credit what goes out

Example: Purchased machinery for cash.
Debit Machinery (comes in), Credit Cash (goes out).

Q11. Explain the golden rule of accounting for nominal accounts with an example.
Ans:
For nominal accounts:
- Debit all expenses and losses
- Credit all incomes and gains

Example: Paid rent of ₹5,000.
Debit Rent Expense, Credit Cash.

Q12. What is the dual aspect concept?
Ans:
The dual aspect concept means every transaction affects two accounts – one account is debited and another credited with equal amounts, maintaining the accounting equation.

☑ 5-Mark Questions

Q13. Define personal accounts and explain their types.
Ans:
Personal accounts relate to persons or entities. Types include:
- Natural persons (e.g., Ram)
- Artificial persons (e.g., companies)
- Representative persons (e.g., outstanding salaries)

Q14. Explain real accounts with examples and their types.

Ans:
Real accounts relate to assets.
Types:

- Tangible assets (cash, machinery)
- Intangible assets (patents, goodwill)
  Examples: Cash Account, Machinery Account.

Q15. Explain nominal accounts and give examples of different types.
Ans:
Nominal accounts deal with expenses, losses, incomes, and gains.
Types:

- Expenses (salary, rent)
- Incomes (commission received, interest)
- Losses (bad debts)
- Gains (profit on sale)

☑ 8-Mark Question

Q16. Write detailed notes on the rules of debit and credit with suitable examples for each type of account.
Ans:

- **Personal Account:** Debit the receiver, Credit the giver.
  Example: Ram gave goods to Shyam on credit. Debit Shyam, Credit Ram.
- **Real Account:** Debit what comes in, Credit what goes out.
  Example: Bought furniture for cash. Debit Furniture, Credit Cash.
- **Nominal Account:** Debit all expenses and losses, Credit all incomes and gains.
  Example: Paid rent. Debit Rent Expense, Credit Cash.

Q17. How does the dual aspect principle govern the rules of debit and credit? Explain.
Ans:
The dual aspect concept states that every transaction has two effects – one debit and one credit, equal in amount, ensuring the accounting equation stays balanced. The debit and credit rules are derived to maintain this principle for different accounts.

Q18. Differentiate between real, personal, and nominal accounts with suitable examples.
Ans:

Account Type	Description	Examples
Real Account	Assets (tangible/intangible)	Cash, Machinery
Personal Account	Persons/Entities	Ram, XYZ Ltd.
Nominal Account	Expenses/Incomes	Salary, Interest

Q19. What is the significance of the rules of debit and credit in accounting?
Ans:
These rules help in the systematic recording of transactions, maintain consistency, ensure correct financial statement preparation, and uphold the dual aspect concept.

Q20. Explain with examples how the rules of debit and credit are applied when a business receives cash from a debtor.
Ans:
Receiving cash from debtor means cash (real account) comes in, debtor (personal account) gives cash.

- Debit Cash Account (what comes in)
- Credit Debtor’s Account (giver)

Chapter 7: Journal

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What is a journal?
Ans:
A journal is a book of original entry where all business transactions are recorded in chronological order before posting to ledger accounts.

Q2. What is the format of a journal?
Ans:
The journal format typically includes Date, Particulars, Ledger Folio (L.F.), Debit amount, and Credit amount.

Q3. Define 'journalizing'.
Ans:
Journalizing is the process of recording transactions in the journal.

Q4. What is a journal entry?
Ans:
A journal entry is a formal record of a business transaction showing debit and credit accounts and amounts.

Q5. What is meant by 'narration' in a journal entry?
Ans:
Narration is a brief description written below a journal entry explaining the nature of the transaction.

☑ 3-Mark Questions

Q6. What are the advantages of journal?
Ans:
1. Provides chronological record of transactions.
2. Helps in identifying errors early.
3. Facilitates easy transfer to ledger accounts.

Q7. State the rules for writing journal entries.
Ans:
- Debit the account receiving benefit.
- Credit the account giving benefit.
- Write date and narration.
- Indent credit entry below debit entry.

Q8. What is compound journal entry? Give an example.
Ans:
A compound journal entry involves more than two accounts (multiple debits or credits).
Example:
Purchased machinery for ₹50,000, paid ₹30,000 in cash and the balance on credit.
Journal:
Debit Machinery ₹50,000
Credit Cash ₹30,000
Credit Creditors ₹20,000

☑ 4-Mark Questions

Q9. How do you record a purchase of goods on credit in the journal?
Ans:

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
xxxx	Purchases A/c Dr.		₹xxxx	
To Creditors A/c			₹xxxx	
(Goods purchased on credit)				

Q10. Explain the difference between journal and ledger.
Ans:

Basis	Journal	Ledger
Purpose	Book of original entry	Book of final entry
Nature	Chronological	Classified
Format	Date, particulars, debit, credit	Separate accounts for each head
Use	First step of recording	Used for preparation of trial balance

Q11. Write a journal entry for receiving cash from debtor ₹5,000.
Ans:

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
xxxx	Cash A/c Dr.		5,000	
To Debtors A/c			5,000	
(Received cash from debtor)				

Q12. What is the significance of narration in a journal?
Ans:
Narration explains the transaction and helps in understanding the nature of the entry. It also aids auditors and future references.

☑ 5-Mark Questions

Q13. Describe the rules for debit and credit in journal entries with examples.
Ans:
Rules:

- Debit the receiver, Credit the giver (Personal Account)
- Debit what comes in, Credit what goes out (Real Account)
- Debit all expenses and losses, Credit all incomes and gains (Nominal Account)

Example:
Paid rent ₹2,000:
Debit Rent Expense, Credit Cash.

Q14. Prepare journal entries for the following transactions:
(a) Purchased goods for ₹10,000 in cash.
(b) Sold goods to Ram on credit ₹15,000.
Ans:
(a)
Purchases A/c Dr. ₹10,000
To Cash A/c ₹10,000
(b)
Ram's A/c Dr. ₹15,000
To Sales A/c ₹15,000

Q15. What is a compound journal entry? Explain with two examples.
Ans:
A compound journal entry involves more than two accounts.
Example 1:
Paid ₹5,000 to creditors and ₹3,000 as rent.
Creditors A/c Dr. ₹5,000
Rent Expense A/c Dr. ₹3,000
To Cash A/c ₹8,000
Example 2:

Purchased machinery ₹50,000, paid ₹30,000 cash and ₹20,000 on credit.
Machinery A/c Dr. ₹50,000
To Cash A/c ₹30,000
To Creditors A/c ₹20,000

☑ 8-Mark Question

Q16. Explain the importance of journal and the rules of debit and credit with suitable examples.
Ans:

- **Importance of Journal:**
  - It is the book of original entry.
  - Maintains chronological record.
  - Helps in locating errors.
  - Facilitates smooth posting to ledger.
- **Rules of Debit and Credit:**
  - Personal Account: Debit receiver, Credit giver.
  - Real Account: Debit what comes in, Credit what goes out.
  - Nominal Account: Debit expenses and losses, Credit incomes and gains.
- **Examples:**
  - Purchased goods on credit: Debit Purchases, Credit Creditors.
  - Paid salary: Debit Salary Expense, Credit Cash.

Q17. What is meant by 'posting'? Explain the relationship between journal and ledger.
Ans:
Posting is the process of transferring entries from the journal to respective ledger accounts. The journal records transactions in chronological order, while ledger organizes them by account for preparation of financial statements.

Q18. How do you correct errors in journal entries? Explain with examples.
Ans:
Errors can be corrected by:

- Making a rectifying journal entry.
- Example: If ₹500 rent was debited as ₹50, rectify by debiting ₹450 rent and crediting ₹450 cash.

Q19. Prepare journal entries for the following:
(a) Paid wages ₹2,000.
(b) Received commission ₹1,000 in cash.
(c) Purchased furniture ₹8,000 on credit.
Ans:
(a)
Wages A/c Dr. ₹2,000
To Cash A/c ₹2,000
(b)
Cash A/c Dr. ₹1,000
To Commission Received A/c ₹1,000
(c)
Furniture A/c Dr. ₹8,000
To Creditors A/c ₹8,000

Q20. Differentiate between simple and compound journal entries with examples.
Ans:

Basis	Simple Journal Entry	Compound Journal Entry
Number of Accounts	Two (one debit, one credit)	More than two accounts
Complexity	Simple and straightforward	Complex, multiple accounts
Example	Paid rent ₹1,000: Debit Rent Expense, Credit Cash	Paid wages ₹2,000 and rent ₹1,000: Debit Wages and Rent Expense, Credit Cash ₹3,000

Chapter 8: Ledger

20 Important Questions with Full Explanations

2-Mark Questions

Q1. What is a ledger?
Ans:
A ledger is a book of final entry where all the journal entries are posted under individual accounts.

Q2. What is ledger posting?
Ans:
Ledger posting is the process of transferring debit and credit amounts from journal entries to the respective ledger accounts.

Q3. What is a ledger folio?
Ans:
Ledger folio (L.F.) is the page number of the ledger account where the entry is posted. It is recorded in the journal for cross-reference.

Q4. Define an account.
Ans:
An account is a statement that shows the changes in assets, liabilities, income, or expenses due to transactions.

Q5. What is the format of a ledger account?
Ans:
The ledger account has two sides: the left side is the Debit side, and the right side is the Credit side. It includes Date, Particulars, L.F., Debit Amount, and Credit Amount.

3-Mark Questions

Q6. What is the purpose of a ledger?
Ans:
The ledger classifies and summarizes transactions recorded in the journal, making it easier to prepare trial balance and financial statements.

Q7. State the differences between journal and ledger.
Ans:

Basis	**Journal**	**Ledger**
Entry type	Book of original entry	Book of final entry
Arrangement	Chronological	Account-wise
Purpose	Recording transactions	Classification and summarization
Format	Single book	Multiple accounts

Q8. Explain the importance of ledger folio.
Ans:
Ledger folio helps to cross-reference between journal and ledger, making it easier to trace and verify entries.

4-Mark Questions

Q9. What is the double-entry system of accounting?
Ans:
The double-entry system means each transaction is recorded twice — once as debit in one account and once as

credit in another, ensuring the accounting equation stays balanced.

Q10. Explain how ledger accounts are prepared from journal entries.
Ans:
From each journal entry, debit and credit amounts are transferred to respective ledger accounts by entering the date, particulars, and amount on the appropriate side (debit or credit).

Q11. Write the ledger format with an example.
Ans:

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
xxxx	To Cash A/c		5,000	
xxxx	By Sales A/c			5,000

Example: Ledger of Debtors Account showing debit and credit entries.

☑ 5-Mark Questions

Q12. Explain the advantages of ledger.
Ans:
- Classifies transactions into accounts
- Helps in preparation of trial balance
- Facilitates error detection
- Summarizes transactions for financial statements

Q13. What is balancing of ledger accounts? Explain with example.
Ans:
Balancing is finding the difference between total debit and credit sides to determine the balance of the account.
Example: If debit side is ₹10,000 and credit side is ₹7,000, balance is ₹3,000 debit.

Q14. What is the relationship between journal and ledger?
Ans:
Journal records transactions first (original entry) and ledger classifies these entries under respective accounts for summarization.

Q15. How does ledger help in the preparation of trial balance?
Ans:
Ledger provides balances of all accounts, which are extracted and listed in the trial balance to check the equality of total debit and credit.

☑ 8-Mark Questions

Q16. Explain the process of ledger posting with examples.
Ans:
Posting involves transferring the debit and credit amounts from the journal to the respective ledger accounts. For example, if the journal entry is:
Cash A/c Dr. ₹10,000
To Sales A/c ₹10,000
Then in Cash Account ledger: debit ₹10,000 with date and particulars.
In Sales Account ledger: credit ₹10,000 with date and particulars.

Q17. Describe the format of a ledger account with a practical illustration.
Ans:
Ledger account format has two sides: debit (left) and credit (right). Date, particulars, ledger folio, and amounts are recorded.
Example: Cash Account:

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
01/06	Capital A/c		50,000	
05/06	To Purchases			10,000

Q18. Differentiate between simple and compound ledger accounts with examples.
Ans:
- Simple ledger has one debit and one credit entry per transaction.
- Compound ledger has multiple debits or credits in a transaction.
  Example (simple): Paid rent ₹2,000 – Debit Rent Expense, Credit Cash.
  Example (compound): Paid wages ₹3,000 and rent ₹2,000 in cash – Debit Wages and Rent Expense, Credit Cash ₹5,000.

Q19. Explain the importance of ledger folio column in journals and ledgers.
Ans:
Ledger folio number records the page of ledger where the entry is posted. It helps in cross-checking and tracing entries between journal and ledger efficiently.

Q20. How do you prepare ledger accounts from journal entries involving purchases on credit? Give an example.
Ans:
Example: Purchased goods on credit ₹15,000 from Ram.
Journal Entry:
Purchases A/c Dr. ₹15,000
To Ram's A/c ₹15,000
Ledger Posting:
- Purchases Account: Debit ₹15,000
- Ram's Account: Credit ₹15,000

📚 Chapter 9: Trial Balance

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What is a trial balance?
Ans:
Trial balance is a statement that lists all ledger account balances to check the arithmetical accuracy of bookkeeping.

Q2. What are the two types of trial balance?
Ans:
1. **Preliminary Trial Balance** – prepared before adjustments.
2. **Adjusted Trial Balance** – prepared after adjustments.

Q3. What is the purpose of preparing a trial balance?
Ans:
To verify that total debit balances equal total credit balances and detect errors in ledger posting.

Q4. What are debit and credit balances?
Ans:
- Debit balance means debit side is more than credit side.
- Credit balance means credit side is more than debit side.

Q5. What is the format of a trial balance?
Ans:
It has three columns: Account Name, Debit Balance, and Credit Balance.

☑ 3-Mark Questions

Q6. What are the errors not disclosed by trial balance?
Ans:
- Errors of omission
- Errors of commission
- Errors of principle
- Compensating errors

Q7. What is the difference between trial balance and balance sheet?
Ans:

Basis	**Trial Balance**	**Balance Sheet**
Purpose	Check arithmetical accuracy	Financial position on a date
Format	List of balances	Statement of assets and liabilities
Timing	Before final accounts	After adjustments

Q8. How is a trial balance prepared?
Ans:
List all ledger account balances on debit or credit side, total both columns, and verify equality.

☑ 4-Mark Questions

Q9. Explain the main objectives of preparing a trial balance.
Ans:
- To verify arithmetical accuracy of ledger posting.
- To assist in preparation of final accounts.
- To detect certain types of errors.

Q10. What are the causes for disagreement in trial balance?
Ans:
- Error of omission
- Error of commission
- Error of principle
- Posting error
- Balancing error
- Transposition error

Q11. Prepare a simple trial balance from the following ledger balances:
Cash ₹10,000 (Dr), Capital ₹50,000 (Cr), Purchases ₹8,000 (Dr), Sales ₹40,000 (Cr).
Ans:

Account	**Debit (₹)**	**Credit (₹)**
Cash	10,000	
Purchases	8,000	
Capital		50,000
Sales		40,000
Total	18,000	90,000

Trial balance does not balance → error to be found.

☑ 5-Mark Questions

Q12. Explain briefly the limitations of trial balance.
Ans:
- Does not detect all types of errors.
- Only checks arithmetic equality, not accuracy of entries.
- Errors of omission and commission remain undetected.

Q13. What is the accounting equation and how does trial balance relate to it?
Ans:
Accounting equation: Assets = Liabilities + Capital.
Trial balance ensures total debits equal total credits, which supports the equation's balance.

Q14. How to rectify errors discovered during trial balance preparation?
Ans:
Identify the error and pass rectification journal entries to correct it.

Q15. Distinguish between errors disclosed and not disclosed by trial balance.
Ans:

Errors Disclosed	Errors Not Disclosed
Posting errors	Errors of omission
Balancing errors	Errors of commission
Transposition errors	Errors of principle
Partial omission	Compensating errors

☑ 8-Mark Questions

Q16. Explain the steps involved in preparing a trial balance with an example.
Ans:
- List all ledger accounts and their balances.
- Enter debit balances in the debit column, credit balances in the credit column.
- Total the debit and credit columns.
- Check if totals are equal.

Example:

Account	Debit (₹)	Credit (₹)
Cash	20,000	
Capital		50,000
Sales		40,000
Purchases	30,000	
Total	50,000	90,000

Unequal totals indicate errors.

Q17. What are compensating errors? Explain with an example.
Ans:
Compensating errors occur when one error is offset by another error of equal amount.
Example:
Overstating purchases by ₹500 and understating sales by ₹500; trial balance totals still match.

Q18. Describe the trial balance errors and how they affect the accounts.
Ans:
- **Error of omission:** Transaction not recorded → totals mismatch.
- **Error of commission:** Wrong account used → trial balance may still balance.
- **Error of principle:** Violation of accounting principles → may not affect trial balance.
- **Compensating errors:** Errors offset each other → trial balance balances.

Q19. Prepare a trial balance from the following information and check if it balances:
Cash ₹12,000 (Dr), Creditors ₹7,000 (Cr), Rent Expense ₹2,000 (Dr), Capital ₹15,000 (Cr), Sales ₹10,000 (Cr), Purchases ₹8,000 (Dr).
Ans:

Account	Debit (₹)	Credit (₹)

Cash	12,000	
Rent Expense	2,000	
Purchases	8,000	
Creditors		7,000
Capital		15,000
Sales		10,000
Total	22,000	32,000

Not balanced → error exists.

Q20. What is the significance of preparing a trial balance in accounting?
Ans:
- Ensures the books are arithmetically correct.
- Helps in detecting errors early.
- Provides a summary for preparing financial statements.
- Saves time in error detection.

📓 Chapter 10: Rectification of Errors

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What is meant by rectification of errors?
Ans:
Rectification of errors means correcting mistakes found in the books of accounts after the trial balance is prepared.

Q2. Name two types of errors that can be rectified.
Ans:
1. Errors disclosed by trial balance
2. Errors not disclosed by trial balance

Q3. What is an error of omission?
Ans:
An error of omission occurs when a transaction is completely omitted from the books of accounts.

Q4. Define compensating errors.
Ans:
Compensating errors occur when one error is offset by another error of equal amount, so the trial balance still agrees.

Q5. What is an error of commission?
Ans:
An error of commission happens when an entry is made in the wrong account but the amount is correct.

☑ 3-Mark Questions

Q6. What is the difference between errors disclosed and errors not disclosed by trial balance?
Ans:

Basis	**Errors Disclosed**	**Errors Not Disclosed**
Trial balance	Does not agree	Trial balance agrees

Examples	Wrong totaling, posting errors	Omission, commission, principle errors

Q7. Explain the effect of errors on the trial balance.
Ans:
Some errors cause the trial balance to be out of balance (disclosed errors), while others do not affect the equality of debit and credit totals (undisclosed errors).

Q8. How is the rectification entry recorded if an error is found before preparing final accounts?
Ans:
The error is corrected by passing a journal entry to adjust the affected accounts.

☑ 4-Mark Questions

Q9. Explain the procedure for rectifying an error discovered after the preparation of trial balance.
Ans:
- Identify the error and affected accounts.
- Pass a rectification journal entry to correct the mistake.
- Adjust the trial balance and final accounts accordingly.

Q10. What is the difference between an error of principle and an error of commission?
Ans:

Error Type	Description	Example
Error of Principle	Violation of accounting principles	Recording capital expenditure as revenue
Error of Commission	Wrong account but correct class	Recording purchase in rent account

Q11. What are the methods of rectification of errors?
Ans:
- **Rectification through journal entries** if error is found before trial balance.
- **Rectification through suspense account** if error is found after trial balance.

☑ 5-Mark Questions

Q12. What is a suspense account and when is it used?
Ans:
Suspense account is a temporary account used when the trial balance does not tally due to errors. It holds the difference until errors are found and corrected.

Q13. Explain how errors of omission can be rectified with examples.
Ans:
If a transaction is omitted completely, it is recorded in the books by passing the correct journal entry.
Example: Goods purchased for ₹5,000 omitted, rectify by:
Purchases A/c Dr. ₹5,000
To Creditors A/c ₹5,000

Q14. Differentiate between errors of omission and errors of commission with examples.
Ans:

Basis	Error of Omission	Error of Commission
Nature	Transaction not recorded	Wrong account used
Effect	Trial balance does not tally	Trial balance may tally
Example	Not recording purchase	Recording purchase in rent account

Q15. What is the impact of compensating errors on trial balance and final accounts?
Ans:
Compensating errors do not affect the trial balance because one error cancels out the other. However, they

distort the true financial position and must be rectified.

☑ 8-Mark Questions

Q16. Describe the steps to rectify errors when the trial balance does not tally using the suspense account method.
Ans:

- Calculate the difference between debit and credit totals.
- Open a suspense account for that difference.
- Pass journal entries to transfer the difference to suspense account.
- Investigate and locate the errors.
- Pass rectification entries to correct the errors and close suspense account.

Q17. Explain with example how to rectify the following errors:
a) A purchase of ₹1,000 was recorded in the sales book.
b) ₹500 paid for repairs was debited to the machinery account.
Ans:
a) Wrong recording:
Sales A/c Dr. ₹1,000
To Purchases A/c ₹1,000
b) Wrong account:
Repairs Expense A/c Dr. ₹500
To Machinery A/c ₹500

Q18. What is a rectification entry? Explain with examples.
Ans:
A rectification entry is a journal entry passed to correct errors in the books of accounts.
Example:
If a receipt of ₹2,000 from a debtor is not recorded, entry will be:
Cash A/c Dr. ₹2,000
To Debtors A/c ₹2,000

Q19. What are the common errors that do not affect the trial balance? Explain with examples.
Ans:

- Errors of omission (completely missed entries).
- Errors of commission (wrong account used but correct side).
- Errors of principle (wrong classification).
  Example: Purchase recorded as rent expense.

Q20. How do errors affect the financial statements? Explain.
Ans:
Errors distort the true profit and financial position. For example, overstating expenses reduces profit, understating assets affects the balance sheet, leading to wrong decision-making.

Chapter 11: Depreciation, Provisions, and Reserves

◇ ***20 Important Questions with Full Explanations***

☑ 2-Mark Questions

Q1. What is depreciation?
Ans:
Depreciation is the gradual and systematic allocation of the cost of a tangible fixed asset over its useful life.

Q2. Define provision.
Ans:
A provision is an amount set aside from profits to meet a known liability or decrease in asset value whose amount is uncertain.

Q3. What is a reserve?
Ans:
A reserve is an appropriation of profits to strengthen the financial position of the business or for a specific purpose.

Q4. Name two methods of calculating depreciation.
Ans:
1. Straight Line Method (SLM)
2. Diminishing Balance Method (DBM)

Q5. Why is depreciation charged on assets?
Ans:
To allocate the cost of the asset over its useful life and reflect true profit and asset value.

☑ 3-Mark Questions

Q6. Differentiate between provision and reserve.
Ans:

Basis	Provision	Reserve
Purpose	To meet known liabilities or asset loss	To strengthen financial position or specific use
Nature	Expense or liability	Appropriation of profit
Impact on Profit	Reduces profit	Reduces distributable profit

Q7. What are the causes of depreciation?
Ans:
- Wear and tear due to use
- Obsolescence due to technology changes
- Expiry of useful life
- Accidents or natural causes

Q8. What is meant by useful life of an asset?
Ans:
It is the estimated period for which the asset is expected to be used productively.

☑ 4-Mark Questions

Q9. Explain the Straight Line Method of depreciation with formula.
Ans:
In Straight Line Method, equal depreciation is charged every year.
Formula:
Depreciation Expense = (Cost of Asset – Scrap Value) / Useful Life

Q10. Describe the Diminishing Balance Method of depreciation with formula.
Ans:
In this method, depreciation is charged at a fixed percentage on the reducing balance (book value) of the asset each year.
Formula:
Depreciation Expense = Written Down Value × Rate of Depreciation

Q11. What are the objectives of creating reserves?
Ans:
- To meet future contingencies
- To strengthen financial position
- To fund future expansion or replacement
- To ensure stability in dividend payments

Q12. How is provision different from contingent liability?

Ans:
Provision is a liability of uncertain amount but likely to occur, while contingent liability depends on occurrence of a future event and is not recorded in books.

☑ 5-Mark Questions

Q13. Explain the importance of charging depreciation in accounting.
Ans:
- Reflects true profit by matching cost with revenue
- Shows true asset value in balance sheet
- Helps in proper pricing of goods
- Facilitates replacement of assets
- Ensures compliance with accounting standards

Q14. Write a short note on 'Provision for Doubtful Debts.'
Ans:
It is a provision created to cover debts which are uncertain to be collected fully. It is shown as a deduction from debtors in the balance sheet.

Q15. What is the difference between capital reserve and revenue reserve?
Ans:

Basis	Capital Reserve	Revenue Reserve
Source	Capital profits (e.g., sale of asset)	Revenue profits (business profits)
Purpose	Non-distributable	Distributable to shareholders
Usage	For writing off capital losses	For business expansion or dividends

Q16. How is depreciation recorded in the books of accounts?
Ans:
Depreciation expense is debited to the Profit & Loss Account and credited to the Accumulated Depreciation Account (or directly to the asset account).

☑ 8-Mark Questions

Q17. A machine costing ₹1,00,000 is purchased with an estimated scrap value of ₹10,000 and a useful life of 5 years. Calculate depreciation for 3 years using:
a) Straight Line Method
b) Diminishing Balance Method at 20%
Ans:
a) Straight Line Method:
Depreciation per year = (₹1,00,000 - ₹10,000) / 5 = ₹18,000
For 3 years = ₹18,000 × 3 = ₹54,000
b) Diminishing Balance Method:
Year 1 = 20% of ₹1,00,000 = ₹20,000; Book Value = ₹80,000
Year 2 = 20% of ₹80,000 = ₹16,000; Book Value = ₹64,000
Year 3 = 20% of ₹64,000 = ₹12,800; Total = ₹20,000 + ₹16,000 + ₹12,800 = ₹48,800

Q18. Explain the concept of 'Provision for Bad Debts' with its importance.
Ans:
Provision for Bad Debts is created to anticipate future bad debts that may arise from debtors.
Importance:
- Matches expense with revenue (prudence)
- Shows realistic debtors balance
- Helps in prudent financial management

Q19. Write a detailed note on 'General Reserve.'
Ans:
General Reserve is an undistributed revenue reserve created to strengthen the financial position. It is used for

unforeseen contingencies, expansion, or debt repayment. It is shown on the liabilities side of the balance sheet.

Q20. How do provisions and reserves affect the financial statements? Explain.
Ans:
- Provisions reduce profits and show as liabilities or deductions from assets.
- Reserves are appropriations of profits and reduce distributable profits.
- Both strengthen the balance sheet by ensuring liabilities and contingencies are accounted for.

Chapter 12: Accounting for Bills of Exchange

20 Important Questions with Full Explanations

2-Mark Questions

Q1. What is a bill of exchange?
Ans:
A bill of exchange is a written, unconditional order directing a person to pay a certain sum of money to another person or to the bearer at a specified future date.

Q2. Define the term 'drawer' and 'drawee'.
Ans:
- Drawer: The person who makes or draws the bill.
- Drawee: The person who is directed to pay the amount.

Q3. What is the 'payee' in a bill of exchange?
Ans:
The payee is the person to whom the payment is to be made.

Q4. What is a promissory note?
Ans:
A promissory note is a written promise made by one person to pay a certain sum of money to another person at a specified future date.

Q5. What is meant by 'acceptance' of a bill?
Ans:
Acceptance is the drawee's written agreement to pay the bill on the due date by signing on it.

3-Mark Questions

Q6. Mention three characteristics of a bill of exchange.
Ans:
- It is a written and unconditional order.
- It contains a definite amount of money.
- It specifies the payment date.

Q7. What are the parties involved in a promissory note?
Ans:
Two parties:
- Maker (who promises to pay)
- Payee (to whom the payment is made)

Q8. Differentiate between a bill of exchange and a promissory note.
Ans:

Basis	Bill of Exchange	Promissory Note
Number of parties	Three parties (Drawer, Drawee, Payee)	Two parties (Maker, Payee)
Nature of instrument	Order to pay	Promise to pay
Acceptance required	Yes	No

☑ 4-Mark Questions

Q9. Explain the term 'due date' in bills of exchange.
Ans:
Due date is the date on which the payment of the bill must be made. It is calculated based on the date of acceptance or date of the bill, depending on the terms.

Q10. What is endorsement? Mention two types of endorsement.
Ans:
Endorsement is the process of transferring the title of the bill by signing on its back. Types:
- Blank endorsement
- Special endorsement

Q11. How is a dishonored bill recorded in the books?
Ans:
When a bill is dishonored, it is returned unpaid by the drawee. The drawer debits the debtor and credits the bills receivable account.

☑ 5-Mark Questions

Q12. Write journal entries for the following transactions:
a) Drawing a bill on a debtor for ₹10,000.
b) Receiving the amount on maturity of the bill.
Ans:
a) Bills Receivable A/c Dr. ₹10,000
To Debtor A/c ₹10,000
b) Cash A/c Dr. ₹10,000
To Bills Receivable A/c ₹10,000

Q13. What is 'discounting of a bill'? How is it recorded?
Ans:
Discounting a bill means getting cash before maturity by paying discount to the bank.
Entry on discounting:
Cash A/c Dr. (amount received)
Discount on Bills A/c Dr. (discount)
To Bills Receivable A/c (full amount)

Q14. Explain the process of 'renewal of a bill'.
Ans:
When a bill is not paid on maturity and both parties agree to extend the payment date, the original bill is cancelled and a new bill is drawn. Journal entry involves writing off the old bill and recording the new one.

Q15. What are the advantages of using bills of exchange?
Ans:
- Facilitates credit sales
- Acts as a proof of debt
- Helps in getting loans against bills
- Provides legal evidence in case of disputes

☑ 8-Mark Questions

Q16. From the following transactions, pass journal entries:
- Sold goods on credit to Raju ₹20,000 and drew a 3 months bill on him.

- On maturity, Raju paid ₹20,000.
- Purchased goods from Sita ₹15,000 and accepted a 2 months bill.
- Paid Sita on maturity by cheque.

Ans:

- Debtor Raju A/c Dr. ₹20,000
  To Sales A/c ₹20,000
- Bills Receivable A/c Dr. ₹20,000
  To Debtor Raju A/c ₹20,000
- Cash A/c Dr. ₹20,000
  To Bills Receivable A/c ₹20,000
- Purchases A/c Dr. ₹15,000
  To Creditor Sita A/c ₹15,000
- Creditor Sita A/c Dr. ₹15,000
  To Bills Payable A/c ₹15,000
- Bills Payable A/c Dr. ₹15,000
  To Bank A/c ₹15,000

Q17. What is 'noting' and 'protest' in relation to bills of exchange?
Ans:

- Noting: Formal recording of dishonor by a notary public.
- Protest: A legal document certifying dishonor after noting.

Q18. Explain the accounting treatment for dishonor of bills receivable.
Ans:
When a bill is dishonored, the amount is debited back to the debtor's account and the bills receivable account is credited. If noting charges are paid, they are debited to debtor's account.

Q19. Describe how bills payable are recorded and settled.
Ans:
Bills payable are credited when accepted. On payment, bills payable is debited and cash or bank is credited. If dishonored, creditor account is debited.

Q20. Explain the difference between trade bills and accommodation bills.
Ans:

Basis	Trade Bills	Accommodation Bills
Purpose	Arise from sale/purchase of goods	Created to help parties financially
Legality	Legal and binding	Not genuine, created without trade
Use	Credit transactions	Temporary financial assistance

📚 Chapter 13: Financial Statements — An Introduction

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What are financial statements?
Ans:
Financial statements are reports prepared at the end of an accounting period to show the financial performance and position of a business.

Q2. Name two main financial statements.
Ans:

1. Trading and Profit & Loss Account
2. Balance Sheet

Q3. What is meant by 'profit' in financial statements?
Ans:
Profit is the excess of revenues over expenses during a particular period.

Q4. What is a trial balance?
Ans:
Trial balance is a statement showing the balances of all ledger accounts to check the arithmetical accuracy of bookkeeping.

Q5. Define 'capital'.
Ans:
Capital is the amount invested by the owner(s) in the business.

☑ 3-Mark Questions

Q6. What is the purpose of preparing financial statements?
Ans:
- To know the financial performance of the business
- To ascertain financial position
- To assist stakeholders in decision-making

Q7. Distinguish between profit and loss account and balance sheet.
Ans:

Basis	Profit & Loss Account	Balance Sheet
Purpose	To show net profit or loss	To show financial position
Components	Revenues and expenses	Assets, liabilities, and capital
Time period	For a specific period	As on a particular date

Q8. What are expenses? Give two examples.
Ans:
Expenses are costs incurred in earning revenue. Examples: Rent, salaries.

☑ 4-Mark Questions

Q9. Explain the term 'liabilities' with examples.
Ans:
Liabilities are obligations or debts owed by the business to outsiders. Examples include loans, creditors, and outstanding expenses.

Q10. What is meant by 'closing stock'? Why is it shown in financial statements?
Ans:
Closing stock is the value of unsold goods at the end of the accounting period. It is shown to accurately calculate gross profit and show current assets.

Q11. What is the importance of preparing a trial balance?
Ans:
- To verify ledger accuracy
- To detect errors
- To prepare financial statements easily

☑ 5-Mark Questions

Q12. What is the difference between capital and revenue expenditure?
Ans:

Basis	Capital Expenditure	Revenue Expenditure
Purpose	To acquire or improve fixed assets	For day-to-day running expenses
Impact on accounts	Shown as asset on balance sheet	Charged to profit & loss account

Q13. Write a short note on 'Gross Profit'.
Ans:
Gross Profit = Net Sales – Cost of Goods Sold (COGS). It shows profit from trading activities before expenses.

Q14. What is meant by 'Net Profit'? How is it calculated?
Ans:
Net Profit is the profit remaining after deducting all expenses from gross profit.
Formula:
Net Profit = Gross Profit – Operating Expenses

Q15. What are the limitations of financial statements?
Ans:
- Do not show qualitative factors
- Based on historical cost
- May contain accounting policies bias
- Ignore inflation impact

☑ 8-Mark Questions

Q16. Prepare a classified balance sheet and explain its components.
Ans:
Classified Balance Sheet groups assets and liabilities into current and non-current.
Components:
- **Assets:** Current (cash, stock) and Non-current (plant, machinery)
- **Liabilities:** Current (creditors, bills payable) and Non-current (loans, capital)

Q17. Explain the preparation of Trading Account and Profit & Loss Account.
Ans:
- **Trading Account:** Shows gross profit by matching direct expenses with sales.
- **Profit & Loss Account:** Shows net profit by adjusting indirect expenses and incomes.

Q18. How are adjustments made for outstanding expenses and prepaid expenses in financial statements?
Ans:
- **Outstanding expenses:** Added to expenses in P&L account and shown as current liabilities.
- **Prepaid expenses:** Deducted from expenses and shown as current assets.

Q19. What is the difference between 'current assets' and 'fixed assets'?
Ans:

Basis	Current Assets	Fixed Assets
Use	Used within one year	Used for more than one year
Examples	Cash, stock, debtors	Land, machinery, building

Q20. Explain the term 'adjustments' in preparation of financial statements. Give examples.
Ans:
Adjustments are entries made to account for income or expenses related to the current period but not recorded.
Examples: Accrued income, outstanding expenses, depreciation.

▧ Chapter 14: Financial Statements of Not-for-Profit Organizations

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What is a not-for-profit organization (NPO)?
Ans:
An NPO is an organization set up for charitable, educational, religious, or social purposes, not aimed at making profits.

Q2. Name two examples of not-for-profit organizations.
Ans:

- Charity trusts
- Educational institutions

Q3. What is a receipt and payment account?
Ans:
A receipt and payment account is a summary of cash and bank transactions (both receipts and payments) during a period.

Q4. What is an income and expenditure account?
Ans:
An income and expenditure account is a summary of revenues earned and expenses incurred during an accounting period to show surplus or deficit.

Q5. Define 'capital fund' in NPOs.
Ans:
Capital fund is the excess of assets over liabilities of an NPO and represents the accumulated funds available for use.

☑ 3-Mark Questions

Q6. Differentiate between receipt and payment account and income and expenditure account.
Ans:

Basis	**Receipt and Payment Account**	**Income and Expenditure Account**
Nature	Real account	Nominal account
Records	All receipts and payments	Revenue income and expenses
Time period	During the year	For a particular accounting year

Q7. What are capital receipts? Give two examples.
Ans:
Capital receipts are those receipts which create liabilities or increase capital. Examples: Donations for building, sale of fixed assets.

Q8. Mention two features of not-for-profit organizations.
Ans:

- No profit motive
- Surplus is reinvested in the organization

☑ 4-Mark Questions

Q9. What is meant by 'surplus' in income and expenditure account?
Ans:
Surplus is the excess of income over expenditure during an accounting period in an NPO.

Q10. How is a receipt and payment account prepared?
Ans:
Receipts and payments account is prepared by recording all cash and bank receipts on the debit side and all payments on the credit side, irrespective of the period to which they relate.

Q11. Explain the treatment of subscriptions in NPO accounts.
Ans:
Subscriptions received during the year are recorded in receipt and payment account; only the amount relating to the current period is shown as income in the income and expenditure account.

☑ 5-Mark Questions

Q12. Write journal entries for the following transactions in NPO:
a) Received subscription ₹50,000 (₹40,000 current year and ₹10,000 advance for next year)
b) Purchased furniture ₹20,000 for office use
Ans:
a) Cash A/c Dr. ₹50,000
To Subscription Received A/c ₹50,000
Adjusting for advance:
Subscription Received A/c Dr. ₹10,000
To Subscription Income A/c ₹10,000
b) Furniture A/c Dr. ₹20,000
To Cash/Bank A/c ₹20,000

Q13. Explain the preparation of income and expenditure account.
Ans:
Income and expenditure account is prepared like a profit & loss account to ascertain surplus or deficit by matching income with related expenses for the period.

Q14. What is meant by 'capital fund' and how is it calculated?
Ans:
Capital fund is the accumulated surplus or deficit.
Calculation:
Capital Fund = Assets – Liabilities

Q15. How are fixed assets treated in the financial statements of an NPO?
Ans:
Fixed assets are recorded in the balance sheet at cost less accumulated depreciation and are not shown in the income and expenditure account.

☑ 8-Mark Questions

Q16. From the following transactions of an NPO, prepare a receipt and payment account:
- Opening cash balance ₹5,000
- Received donation ₹20,000
- Received subscription ₹15,000 (includes ₹3,000 advance)
- Paid salaries ₹8,000
- Purchased furniture ₹10,000
- Received interest ₹2,000
- Paid electricity bill ₹1,000

Q17. Explain the difference between capital receipts and revenue receipts with examples in NPOs.
Ans:

Basis	Capital Receipts	Revenue Receipts
Nature	Create liabilities or capital	Regular income
Examples	Donations for building, grants	Subscription, entrance fees

Q18. Explain the meaning and importance of 'adjustments' in NPO accounts.
Ans:
Adjustments ensure income and expenses are recorded in the correct period. For example, outstanding expenses and prepaid incomes are adjusted to show true surplus or deficit.

Q19. What is the role of an income and expenditure account in an NPO?
Ans:
It shows the financial performance by determining surplus or deficit, helping management make informed decisions.

Q20. What are the key differences between financial statements of profit-making and not-for-profit organizations?
Ans:

Aspect	Profit-Making Organizations	Not-for-Profit Organizations
Objective	To earn profit	To provide service
Financial statements	Trading Account, P&L Account, Balance Sheet	Receipt & Payment, Income & Expenditure Account, Balance Sheet
Profit/Surplus	Profit shown in P&L	Surplus shown in income & expenditure account

📓 Chapter 15: Accounts from Incomplete Records (Single Entry System)

◇ ***20 Important Questions with Full Explanations***

☑ 2-Mark Questions

Q1. What is an incomplete record?
Ans:
Incomplete record means that the business does not maintain a full double-entry bookkeeping system and records are partial or incomplete.

Q2. Define single entry system.
Ans:
Single entry system is a bookkeeping method where only one aspect of each transaction is recorded, mostly cash receipts and payments.

Q3. What are the main features of single entry system?
Ans:
- Records mainly cash transactions
- Does not maintain ledger accounts fully
- No trial balance preparation

Q4. Mention two limitations of the single entry system.
Ans:
- Difficult to ascertain true profit or loss
- No complete record of assets and liabilities

Q5. What is meant by 'debtors' and 'creditors'?
Ans:
Debtors are customers who owe money to the business, and creditors are suppliers to whom the

business owes money.

☑ 3-Mark Questions

Q6. How is profit calculated from incomplete records?
Ans:
Profit can be calculated by preparing a statement of affairs and a capital comparison or using the net worth method.

Q7. What is a statement of affairs?
Ans:
A statement of affairs is a statement showing the assets and liabilities of a business on a particular date to ascertain capital.

Q8. Differentiate between single entry system and double entry system.
Ans:

Basis	Single Entry System	Double Entry System
Records	Partial records	Complete records
Transactions recorded	Only one side	Both debit and credit sides

☑ 4-Mark Questions

Q9. Explain the term 'net worth method' for finding profit.
Ans:
Net worth method calculates profit by comparing opening capital with closing capital adjusted for additional capital introduced and drawings.

Q10. What are the components of statement of affairs?
Ans:
Statement of affairs includes:
- Assets: cash, debtors, stock, furniture, etc.
- Liabilities: creditors, loans, outstanding expenses, etc.

Q11. How do you adjust for drawings in calculating profit from incomplete records?
Ans:
Drawings reduce the owner's capital and must be deducted while calculating closing capital to find profit.

☑ 5-Mark Questions

Q12. From the following data, calculate profit using net worth method:
- Opening capital ₹50,000
- Closing capital ₹70,000
- Additional capital introduced ₹10,000
- Drawings ₹5,000

Ans:
Profit = Closing Capital – Opening Capital + Drawings – Additional Capital
= 70,000 – 50,000 + 5,000 – 10,000 = ₹15,000

Q13. What is the importance of preparing a statement of affairs in single entry system?
Ans:
Statement of affairs helps to:
- Ascertain capital at a given date
- Calculate profit or loss
- Know financial position of the business

Q14. How are outstanding expenses and prepaid expenses treated in incomplete records?
Ans:

- Outstanding expenses are added to expenses in profit calculation
- Prepaid expenses are deducted from expenses

Q15. Explain the process of converting single entry into double entry system.
Ans:
Convert by preparing ledger accounts, trial balance, and final accounts using available data and additional adjustments for missing information.

☑ 8-Mark Questions

Q16. Prepare a statement of affairs from the following information:
Assets: Cash ₹10,000, Debtors ₹20,000, Stock ₹15,000, Furniture ₹5,000
Liabilities: Creditors ₹18,000, Loan ₹7,000

Q17. From the following, calculate profit for the year using net worth method:
Opening assets ₹80,000; Opening liabilities ₹30,000
Closing assets ₹1,20,000; Closing liabilities ₹40,000
Capital introduced ₹20,000; Drawings ₹10,000

Q18. Explain the difficulties faced in maintaining accounts under the single entry system.
Ans:
- Incomplete information
- Difficulty in ascertaining true profit
- Errors are hard to detect
- No system of trial balance

Q19. From the following, prepare a statement of profit or loss and a balance sheet:
Opening capital ₹40,000; Closing capital ₹55,000
Additional capital introduced ₹5,000; Drawings ₹3,000

Q20. What adjustments would you make for outstanding income and income received in advance in incomplete records?
Ans:
- Outstanding income: added to income in profit calculation
- Income received in advance: deducted from income

Chapter 16: Accounting Ratios

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What is an accounting ratio?
Ans:
An accounting ratio is a numerical relationship between two items in financial statements, expressed as a fraction or percentage.

Q2. Name two types of accounting ratios.
Ans:
- Liquidity Ratios
- Profitability Ratios

Q3. Define current ratio.
Ans:
Current ratio = Current Assets ÷ Current Liabilities. It shows the ability to pay short-term obligations.

Q4. What does a high debt-equity ratio indicate?
Ans:
It indicates the business has more debt relative to equity, which means higher financial risk.

Q5. What is the formula for gross profit ratio?
Ans:
Gross Profit Ratio = (Gross Profit ÷ Net Sales) × 100

✅ 3-Mark Questions

Q6. Explain the importance of accounting ratios.
Ans:
- Help in analyzing financial health
- Assist in decision making
- Compare performance over periods or with other companies

Q7. Calculate current ratio from the following:
Current Assets = ₹50,000; Current Liabilities = ₹25,000
Ans:
Current Ratio = 50,000 ÷ 25,000 = 2:1

Q8. What is the significance of the inventory turnover ratio?
Ans:
It measures how quickly inventory is sold and replaced, indicating efficiency in stock management.

✅ 4-Mark Questions

Q9. Explain the difference between liquidity ratios and solvency ratios.
Ans:

Aspect	Liquidity Ratios	Solvency Ratios
Purpose	Measure short-term ability to pay debts	Measure long-term financial stability
Examples	Current Ratio, Quick Ratio	Debt-Equity Ratio

Q10. Calculate gross profit ratio if gross profit is ₹30,000 and net sales are ₹1,50,000.
Ans:
Gross Profit Ratio = (30,000 ÷ 1,50,000) × 100 = 20%

Q11. What is the formula for debt-equity ratio? What does it measure?
Ans:
Debt-Equity Ratio = Long-term Debt ÷ Shareholders' Equity
It measures the relative proportion of debt and equity financing.

✅ 5-Mark Questions

Q12. Calculate the quick ratio from the following data:
Current Assets ₹60,000 (Inventory ₹20,000); Current Liabilities ₹30,000
Ans:
Quick Ratio = (Current Assets – Inventory) ÷ Current Liabilities
= (60,000 – 20,000) ÷ 30,000 = 40,000 ÷ 30,000 = 1.33:1

Q13. Explain how profitability ratios are useful to a business.
Ans:
Profitability ratios help assess the ability of a business to generate profits, efficiency in operations, and overall financial performance.

Q14. What does a current ratio of 1:1 indicate?
Ans:
It indicates that current assets are just enough to cover current liabilities, which may be risky for liquidity.

Q15. Describe the debt-equity ratio and its ideal range.
Ans:
Debt-equity ratio indicates financial leverage. An ideal range is usually between 1:1 to 2:1, meaning balanced financing by debt and equity.

☑ 8-Mark Questions

Q16. From the following data, calculate:
a) Current Ratio
b) Quick Ratio
c) Gross Profit Ratio
d) Debt-Equity Ratio
Data:
Current Assets = ₹80,000; Inventory = ₹30,000; Current Liabilities = ₹40,000; Gross Profit = ₹25,000; Net Sales = ₹1,00,000; Long-term Debt = ₹50,000; Equity Capital = ₹1,00,000

Q17. Explain the significance of liquidity ratios for a business.
Ans:
Liquidity ratios measure the ability of a business to meet short-term obligations. They are crucial for maintaining day-to-day operations and avoiding insolvency.

Q18. Discuss the limitations of accounting ratios.
Ans:
- Based on historical data, not future projections
- Different accounting policies affect comparability
- Ratios alone do not provide complete information
- External factors not considered

Q19. How can ratio analysis help investors and creditors?
Ans:
Investors use ratios to assess profitability and growth potential; creditors analyze liquidity and solvency to evaluate creditworthiness.

Q20. Calculate inventory turnover ratio from the following:
Cost of Goods Sold = ₹90,000; Average Inventory = ₹15,000
Ans:
Inventory Turnover Ratio = Cost of Goods Sold ÷ Average Inventory
= 90,000 ÷ 15,000 = 6 times

▧ Chapter 17: Cash Flow Statement

◇ *20 Important Questions with Full Explanations*

☑ 2-Mark Questions

Q1. What is a cash flow statement?
Ans:

A cash flow statement is a financial statement that shows the inflow and outflow of cash and cash equivalents during a period.

Q2. Name the three main activities in a cash flow statement.
Ans:
- Operating activities
- Investing activities
- Financing activities

Q3. Define 'cash equivalents'.
Ans:
Cash equivalents are short-term, highly liquid investments that can be converted into cash immediately, like treasury bills and money market funds.

Q4. Why is cash flow statement important?
Ans:
It helps assess the liquidity position and cash management of a business.

Q5. What is the difference between cash flow and profit?
Ans:
Cash flow refers to actual cash movement, while profit is the accounting surplus after expenses.

☑ 3-Mark Questions

Q6. Explain operating activities with examples.
Ans:
Operating activities include transactions related to the main business operations, like cash received from customers and cash paid to suppliers.

Q7. What are investing activities? Give two examples.
Ans:
Investing activities involve purchase or sale of fixed assets or investments. Examples: purchase of machinery, sale of land.

Q8. What are financing activities? Give two examples.
Ans:
Financing activities relate to raising or repaying capital. Examples: issuing shares, repayment of loans.

☑ 4-Mark Questions

Q9. Explain the difference between direct and indirect methods of preparing cash flow statements.
Ans:

Aspect	**Direct Method**	**Indirect Method**
Presentation	Shows actual cash receipts and payments	Starts with net profit and adjusts non-cash items
Popularity	Less commonly used	More commonly used

Q10. How is depreciation treated in the cash flow statement?
Ans:
Depreciation is a non-cash expense and is added back to net profit in the indirect method.

Q11. What is the purpose of preparing a cash flow statement?
Ans:
To provide information about cash inflows and outflows, helping stakeholders assess liquidity and financial flexibility.

☑ 5-Mark Questions

Q12. From the following data, prepare a cash flow from operating activities using the indirect method:
Net Profit ₹1,00,000; Depreciation ₹20,000; Increase in Debtors ₹10,000; Decrease in Creditors ₹5,000

Q13. What do you understand by 'net cash flow from financing activities'?
Ans:
It represents net cash received or paid from borrowing, repayment of loans, issuing or buying back shares.

Q14. How are dividends treated in the cash flow statement?
Ans:
Dividends paid are shown as cash outflow under financing activities.

Q15. Explain how changes in working capital affect cash flow from operating activities.
Ans:
Increase in current assets reduces cash flow, while increase in current liabilities increases cash flow.

☑ 8-Mark Questions

Q16. Prepare a cash flow statement from the following information:
Opening cash balance ₹20,000; Closing cash balance ₹30,000; Net Profit ₹1,50,000; Depreciation ₹30,000; Increase in Debtors ₹20,000; Decrease in Creditors ₹10,000; Purchase of machinery ₹40,000; Issue of shares ₹50,000; Loan repayment ₹25,000; Dividends paid ₹10,000.

Q17. Explain the steps involved in preparing a cash flow statement using the indirect method.
Ans:
- Start with net profit
- Add non-cash expenses (depreciation)
- Adjust for changes in working capital
- Include cash flows from investing and financing activities
- Calculate net increase/decrease in cash and cash equivalents

Q18. Discuss the significance of cash flow statements to investors.
Ans:
Investors use cash flow statements to evaluate liquidity, sustainability, and financial health before investing.

Q19. How are non-cash transactions treated in cash flow statements?
Ans:
Non-cash transactions are excluded from cash flow statements as they do not affect actual cash.

Q20. Explain the relationship between cash flow statement and balance sheet.
Ans:
Cash flow statement explains changes in cash balances reported in the balance sheet from one period to another by analyzing cash inflows and outflows.

1. ions.
2. **Create a mini "Accounting File"**:
   - Include source vouchers
   - Ledger posting
   - Trial balance
   - Final Accounts
   - Cash Flow Statement
3. **Analyze real-life data**: Collect financial data from a local shop (with permission), prepare statements, and extract key ratios and interpretations.
4. **Convert single-entry records**: Take a set of incomplete records and develop full double-entry accounting plus final statements.