



Short Answer Type Questions:

Q1. Why is it necessary for accountants to assume that business entity will remain a going concern?

Answer : Going Concern Concept assumes that the business entity will continue its operation for an indefinite period of time. It is necessary to assume so, as it helps to bifurcate revenue expenditure (i.e. expenditure related to current year), and capital expenditure (i.e. expenditure whose benefits accrue over a period of time). For example, a machinery that costs Rs 1,00,000, having an expected life of 10 years, will be treated as a capital expenditure, as its benefit can be availed for more than one year; whereas, the per year depreciation of the machinery, say Rs 10,000, will be regarded as a revenue expenditure.

Q2. When should revenue be recognised? Are there exceptions to the general rule?

Answer : Revenue should be recognised when sales take place either in cash or credit and/or right to receive income from any source is established. Revenue is not recognised, in case, if the income or payment is received in advance or the payment is actually received from the debtors. In a nutshell, revenue will be recognised when the right to receive income is established. For example, Mr. A sold goods in January and received payment in February; then revenue is considered to be recognised in the month of January and not in February. However, if Mr A received cash in advance, i.e. in December and goods are sold in January, then the revenue is recognised in January and not in December.

The exceptions to this rule are given below.

- 1) Hire purchase- When goods are sold on hire-purchase system , the amount received in instalments is treated as revenue.
- 2) Long term construction contract- The long term projects like construction of dams, highways, etc. have long gestation period. Income is recognised on proportionate basis of work certified and not on the completion of contract.

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