Important terms in Accountancy

Transaction

The term 'transaction' refers to any event which is measurable in terms of money, and which brings about a change in the financial position of a person or firm or an economic institution.

Capital

The owner's interest in the assets of the business is usually called capital. It is the difference between what the business owns and what it owes.

Drawings

Any cash or goods taken by the owner for personal use or any private payments made out of business funds are known as drawings.

Assets

Assets are economic resources which are owned by a business and are expected to benefit future operations. Assets may have definite physical form, such as buildings, machinery or merchandise. On the other hand, some assets exist not in physical or tangible form but in the form of valuable legal claims or rights — examples are : amounts due from customers, investments in government bonds, and patent rights. Assets have economic value because they contain service benefits that can be used in future operations or sold to somebody else.

Liabilities

Liabilities are the debts owed by a business to outside parties (called creditors). Liabilities include such things as amounts owed to suppliers for goods or services purchased on credit, amounts borrowed from banks or other lenders, amounts owed to employees for salaries and wages, and taxes due but not yet paid. Discharge of liabilities requires either an outlay of assets (usually cash) or the performance of future services.

Receipts

Receipts denote inflow of cash or cash equivalent from any source.

Payments

Payments denote outflow of cash or cash equivalent for any purpose.

Revenue

Revenue may be defined as the inflow of cash or other assets resulting from the sale of goods and services in the ordinary course of business. Other types of revenue are interest received on investments, commission received, rent received, etc. Revenue causes an increase in capital. The inflow of cash and other assets from customers increases the total assets of the business ; on the other side of the accounting equation, the liabilities do not change, but the capital is increased to match the increase in total assets. Thus revenue is the gross increase in capital resulting from business activities.

Expenses

Expenses may be defined as the cost of the goods and services used up in the process of obtaining revenue. Examples include the cost of goods sold, wages and salaries of employees, charges for newspaper advertising and for telephone services and the wearing out (depreciation) of the building and office equipment. All these items are necessary to attract and serve customers and thereby to obtain revenue. Expenses cause the owner's capital to decrease.

Expenditure

Expenditure is the amount spent for acquiring an asset. It may be for cash or transfer of other assets or on credit. Nearly all expenditure ultimately become expense over the life of an enterprise. That part of the expenditure which has been consumed for the purpose of earning revenue of a particular accounting period is the expense of that accounting period.

Income

The excess of revenue over expense is called income. One should not confuse revenue with income. As stated earlier revenue is the inflow of cash or other assets resulting from the sale of goods and services in the ordinary course of business.

Gains

A gain is the monetary benefit or advantage resulting from a transaction or group of transactions. A gain is different from a profit. Gains are the results of transactions not directly related to the normal revenue-producing activities of the firm.

Losses

A loss is a depletion or decrease in the value of any asset without resulting in any revenue or benefit. For example, loss due to fire, theft etc. It is also used to describe the results of a business when the expenses incurred for a particular period exceed the revenue earned in that period. A loss is different from an expense. An expense brings some benefit, but a loss does not.

Goods

Commodities in which a trader deals are called 'goods' or 'merchandise'. Goods are purchased for resale at a profit. For example, furniture will be the goods for a furniture dealer or cloth will be the goods for a cloth merchant. Goods may be sold either as such or after conversion into finished products.

Purchases

Goods bought by a business are usually referred to as purchases. If the price is paid immediately it is a cash purchase. If the payment is deferred to a future date it is a credit purchase.

Sales

Goods sold by a business are usually referred to as 'sales'. If the sale is for immediate cash it is a case of cash sale ; if the payment is not immediate it is a case of credit sale.

Note : The terms 'purchases' and 'sales' are used in a narrow sense in accounting. They refer only to purchase and sale of goods or merchandise, i.e., commodities in which the business deals. The terms are not applied to items which are not meant for resale.

Returns outward (purchase returns)

These are goods returned to the supplier out of purchases made earlier for reasons such as defective quality, error, over supply etc.

Returns inward (sales returns)

These are goods returned by the customers out of the sales made earlier for reasons such as defective quality, error, over supply.

Import

The term 'import' is used for goods brought in from a foreign country for purposes of trade.

Export

The term 'export' is used for goods sent to a foreign country for purposes of trade.

Freight

Freight is the charge made for conveyance of goods by railways, by water or by sea.

Carriage

Carriage is the charge made for conveyance of goods by land from one place to another, particularly by motor-lorry transport.

Cartage

Cartage is the charge made for conveyance of goods by carts from docks to warehouses, and also from warehouses to docks.

Carriage inwards

All conveyance charges (whether freight, carriage or cartage) paid on goods purchased are called carriage inwards.

Carriage outwards

All conveyance charges (whether freight, carriage or cartage) paid on goods sold are called carriage outwards.

Stock

Unsold goods lying with a business on any given date are called stock. For a manufacturing firm, stock may consist of raw materials, work-in-progress and finished goods. A retailer's stock would normally be only finished goods. Stock at the beginning of an accounting period is called opening stock and that at the end of an accounting period is called closing stock.

Accounts receivable B/R

Accounts receivable are the amounts owed by credit customers for the sale of goods and services. Also called trade debtors or sundry debtors.

Accounts payable B/P

Accounts payable are the amounts owed to suppliers for the purchase of goods and services. Also called trade creditors or sundry creditors.

Debtors

Debtors are persons who owe money to the business, i.e., the persons from whom the business has to recover money. A trade debtor is a person who owes money for sale of goods and services on credit.

Creditors

Creditors are persons to whom the business owes money i.e., the person to whom business has to pay money. A trade creditor is a person to whom the business owes money for purchase of goods and services on credit.

Bad debts

Bad debts are debts which are irrecoverable and should be written-off and debited to the profit and loss account as an expense.

Bills of exchange

A bill of exchange is a written order to pay a sum of money to a certain person or his assignee at a given date. It is a negotiable instrument and passes from hand to hand by endorsement.

Bills payable

Bills payable is an accounting term for bills of exchange accepted in favour of creditors. The amount specified in such a bill is payable at a future date.

Bills receivable

Bills receivable is an accounting term for bills of exchange drawn on debtors or received by way of endorsement from them. The amount specified in such a bill is receivable at a future date.

Investments

Investments are assets representing shares and debentures of companies or securities of financial institutions or the Government. These are not expected to be converted into cash within a year.

Discount

Discount is an allowance or a concession offered by a trader to his customers either for making prompt payment or for bulk purchase.

Trade discount

Trade discount is a deduction allowed by the wholesaler or manufacturer to the retailer from the retail selling price as shown in the wholesaler's or manufacturer's price list. It enables the retailer to sell at the 'list price' and at the same time make a profit.

Cash discount

Cash discount is a deduction allowed from the amount payable by a debtor to encourage prompt payment.