

Chapter 1

Introduction of Accountancy

Learning Objectives:

- 1) Students will be able to understand the meaning of Book keeping and Accountancy.
- 2) To relate Accountancy with other subjects.
- 3) To understand the main features of Single Entry System, Double Entry System and Indian System of Accounting.
- 4) To become familiar with basic Accounting terminology.
- 5) To describe basic Accounting concepts, Assumptions and Conventions.

1.1 Accountancy: An Introduction

If we want to understand accountancy, we should understand Accounting and Book keeping. Accountancy is a special area of knowledge; where Accounting is a process or practice, which is used in Accountancy. Book-keeping is the base of Accounting. So we can say that Book –keeping is the first step and Accounting is the second step of Accountancy. Accounting is based on rules and principles which are established by Accountancy.

It is believed that Accountancy started was with Human Civilisation. Development of Business Trade and Industry continued with the development of Human Civilisation. So this promoted the necessity of Accounting. Human mind has a limited capacity to memorize the things and in trade and business so many transactions occur. So it is not possible for a normal human mind to remember everything. So he started writing these transactions. There is a very old proverb in Hindi “Pahalelikhpiche de, Bhoolpade to kagaj se le.”

In Ramcharita Manas wrote by Goswami Tulsi Das used the word 'Lekha' word. Lines.. यथा "Jitehu Surasur Tab Shram Nahi, Nar Vanar Kehi Lekhe Mahi."

(5-37-9)

Apart from this, many old and famous literatures used this word. All these things clarified that Accounting is used from ancient period. There were changes from time to time according to necessity. In present time, due to use of computer, Accountancy is more modern , fast, accurate and continued. In future Accountancy will be paperless. All transactions will be secured in computer and the work will become less expensive and less turbulent.

1.2 Meaning of Book keeping

Book keeping refers to recording of business transactions in books of accounts. Book keeping is the first part of Accounting. In this we include all those transactions which are related to trade and can be measurable in money value.

According to J. R. Batalibay “Book keeping is an art of recording business dealing in a set of books.”

* In a business recognized those transactions which can be measured in money term. Non-monetary and the transactions which cannot be measured in money terms are not the part of book-keeping.

* Recognising business transactions and write them in books of accounts. After that classified them and post them in ledger.

Book-keeping is a routine work and this work can be done by non- experts or clerks. This work does not require any special skills and knowledge. That is the reason to say book-keeping is the first step of Accounting.

1.3 Meaning of Accounting

When book keeping is complete, the work of Accounting starts. The following works are done in accounting :

- To know the summary of classified transactions, preparation of the Trading, Profit & Loss a/c and Balance Sheet and business results.
- Analysis and interpretation of financial results and providing useful information to concerned persons who has the interest in the results , like government, society, shareholders, employees, management etc.
- Form this analysis prepare useful information and provide them to concern persons.

So, Accounting is the second step of Accountancy, which is based on Book-keeping. Accounting work requires more skills and ability. This work is done by more qualified and skilled persons like Accountant or Accounts officers, because Accounting is based on some specific concepts and principles. This work is more dynamic and analytical. However in small business units Book-keeping and Accounting can be done by the same person.

1.4 Objectives of Book-keeping and Accounting:

There are some common objectives :

- To recognize those business transactions which have monetary value.
- To record these transactions in books of accounts in a systematic manner.
- To classify the transactions and post them in ledger.
- To check the mathematical accuracy in recording of business transactions.
- To calculate net profit/ loss during a specific time period (generally it is 12 months or one year) so that business financial position can be measured.
- To provide systematic and summarized information to management and show proper ability and skill of management.
- To provide financial results and related information to its users.
- To provide a systematic accounting records to help in the settlement of tax liabilities.

- To fulfil legal requirement and help the management by Accounting.

1.5 Accounting as an Art and Science

Accounting is an art as well as a science. Art means way of doing work in any special manner. In Accounting, transactions are written in books of accounts in a special manner, classified them and get the results. And these results are provided to users in a specific manner. It requires creativity so that we can say that Accounting is an Art.

Science is based on certain rules, principles and procedures. In this the presentation and interpretations are also done in certain manner. Accounting is also based on rules and principles. Transactions are properly checked then written in the books and posted in Ledgers. We use a systematic process to find out results of trading activities and financial position so that Accounting is a science also. So we can say that Accounting has the qualities of Art and Science both.

1.6 Difference between Book Keeping and Accounting

Book-keeping and Accounting both are important factors for Accountancy. All business transactions are written in books of Accounts in book-keeping, so it is called first step of Accountancy. And after the completion of this, the work of Accounting starts. The main differences are...

Book-keeping	Accounting
It is primary stage.	It is secondary stage.
It identifies the financial transactions of business.	It summarizes the classified transactions.
Measuring the transactions in money terms and records them in to books of accounts.	Analysis the financial transactions, Preparation of Profit & Loss a/c and Balance Sheet to know the results of business activities.
The main objective is to maintain systematic records of identified transactions in books of accounts.	The objective is to calculate profitability and financial position of the business.
It is a routine work so it does not require special skills.	It is an analytical process so requires special skills.
A normal educated person can do this work.	This work is done by skilled and experienced persons like an Accountant.
It is the base of Accounting.	Accounting begins where book - keeping ends

With above differentiation we can say that Book-keeping is the primary work which provides basic information for Accounting.

1.7 Types or Sub-fields of Accounting

In modern time business, trade and industry are developing day by day. So it increases challenges in front of management. For this only basic information of Accounts are not sufficient. Management requires information in various forms, so that it can fulfil its responsibilities. For this we have several branches of Accounting. These are :

1) Financial Accounting

The basic purpose of financial Accounting is the recording of business transactions, classifying, summarizing and interpreting them by preparing Trading and Profit & Loss Account and getting the financial position of the firm by Balance Sheet. So that useful information can be communicated to various users' such as society, government, shareholder, creditors, customers etc. It is beneficiary for all types of business institutions. In many institutions like a company it is legally compulsory also.

2) Cost Accounting

The main objective of this branch is to calculate cost per unit of the product or services with information provided by the enterprise. In this branch we estimate the cost and compare it with actual cost so that the cost can be reduced and controlled. Low cost can increase the profit volume of the firm.

3) Management Accounting

Management operates the activities of business. For effective operation of these activities management requires accounting information in such a way that Management can fulfil its responsibilities. The main work of management is decision making. The success of decision is based on useful information. Collection of information and analysis and using them in decision making is called management accounting.

4) Social Accounting

A business gets resources for the business from society like Capital, Raw material, Human labour etc. So it is the responsibility of business to work for the society also. The report which shows to what extent social work is done by business is called Social Accounting.

1.8) Accounting and Other Discipline:

To understand the Accounting in a better way ,we should have the knowledge of other disciplines also specially Maths, Statistics, Economics, Management, Law etc. The relationship between these disciplines and Accounting is :

1) Accounting & Mathematics

We have to do many calculations in Accounting. Basic knowledge of addition, subtraction, multiplication and division is obtained from Mathematics only. So it establishes the relation between both the subjects. The adjustment of historical financial figure with inflation a person can

better understand current financial position in a better way. So the person who does the accounting work should have knowledge of maths. Otherwise he will face the difficulty in doing his work. In calculation of interest, Profit & loss, commission, net value of assets and liabilities Maths will be of much help.

2) Accounting & Statistics

In Accounting, information are summarized, analysed, interpreted and presented. For a better presentation we use graphs, charts, figures etc. They all are based on principle of statistics . A person can do accounting work more efficiently with the knowledge of Statistics. So Accounting and Statistics have strong relationship.

3) Accounting & Management

Management requires accounting information to take decision. Accountant is the member of management team. So he should have knowledge, that which type of information is required for management and when it is required. So accountant collects the information according to requirements of management. Accounts have primary information regarding financial issues of business . So with the knowledge of management, accountant can analyse information in proper way and can help the management. Like that Management and Accounting have an old relationship.

4) Accounting and Economics

Accounting and Economics have very important relationship. Many important concepts like concept of income, concept of profit, concept of capital etc can be understood by knowledge of Economics. In Economics capital is like a tree and income and profits are its fruits. So the person, who does accounting work, should have knowledge of principles and rules of Economics. With the help of opening and closing balance of capital ,we can calculate profit or loss in Economics. So principles of Economics are very important for Accounting.

5) Accounting and Law

There are many laws and legal formalities which are used to prepare financial statements, otherwise it lead to penalties and fines. So Accountant should have proper knowledge of laws which are related to Accounting. For example Company Law, Income tax Law, Law related to sales, production and distribution. Law related to labour and bonus etc are important for Accounting. If they are not followed, it may lead to many monetary and non - monetary penalties. So knowledge of both stream is important.

6) Accounting and Sociology

Society provides resources for all business transactions. For this, society expects from business that it will provide best services and products for low price. This process is called social cost befit analysis. It is the responsibility of business to do effort to fulfil the requirements of society. Sociology provides the knowledge of social frame of mind and expectations. Society and

business both are complementary to each other. Business can fulfil its social responsibility by Accounting. There should be a share in net profit for social welfare which should be utilised for social service. So Accounting and Sociology have strong relationship.

1.9) System or Types of Accounting

Basically Accounting is divided in two parts.

- 1) Single Entry System of Accounting
- 2) Double Entry System of Accounting

Apart from this, Indian Accounting System is also do very old and considered as a part of Accounting. It also proved as a reliable and systematic system. Firstly, let us discuss Single Entry System.

1) Single Entry System of Accounting

Generally small businessmen and institutions do not record all business transactions, because they do not feel its requirement. They calculate their financial results on their own basis which is sufficient for them in normal way.

Basically these businessmen and institutions take these records by their bank pass book, personal accounts and ledger. These records are not large but according to their requirement. It is called Single Entry System. Basically there is no such type of accounting system so it is called incomplete record system.

In this system Profit & Loss is calculated according to available records. But it is not complete, so proper and systematic Trading and Profit & Loss account can-not be prepared and after the end of specific period to know the financial situation of firm, it is not possible to make Balance Sheet and without this, only statements of affairs is prepared. These works fulfil only limited objectives of a businessman.

As it is said before, it is beneficial only for small businessman and institutions. It is a very simple and less expensive technique to maintain financial records which requires limited skills. It does not require heavy books of accounts and special skills. But it is not very reliable and not considered in court as legal and reliable proof. It does not have any principles and concepts. It is only for personal satisfaction. It is only based on original vouchers.

In short Single Entry System includes:-

- Only personal accounts and ledger are prepared.
- This system is based on some facts. For example to calculate the purchase of the year business man cross-checks it with the bills received from sellers and suppliers. Similarly for the estimation of sales of the year, it is checked by selling bills which were issued by himself.

- It is not a universal concept. Record of one businessman is not similar to others. Someone have records so much information and other can have less.
- It is easy to understand, less expensive and flexible for small businessman.

There are many drawbacks in Single Entry System. It is an incomplete, unscientific and complex technique. The results are not so reliable. So income tax department, sales tax department and other government and semi government departments, courts etc. donot consider its results. This technique has limited scope and become fails with the growth of the business.

In present time Accountancy is developing continually. So for proper similarity, comparability, accuracy the Accounting Standards are increased. Accounting Standards increases the faith of people towards Accountancy. These are legally compulsory for many business organisations. Specially in company form it is very important in India.

accounting work. So it is not possible to use Accounting Standards in this system. Due to this drawback this system can-not be used by a large business unit.

2) Double Entry System

As an opposite form of Single Entry System, Double Entry System contains full records of business transactions. Each business transactions have two aspects. The transactions are recorded for both aspects. In this system all accounts like Personal, Real and Nominal account are written in systematic manner. This system maintains a complete record of all business transactions. So profit and loss can be calculated scientifically and Balance Sheet can be prepared to know the financial situation of firm. It helps in establishing arithmetical accuracy by preparing a Trial balance. Trading and Profit & Loss a/c are made by primary books of accounts and adjustments can be made for final accounts. It is a scientific and reliable system. It is useful for all types of business organisation. In this system all accounting work is based on principles and concepts. Further we will discuss it in detail. In this system accounts are written in English.

3) Indian System of Accounting

Indian System of Accounting has a special position in Indian culture. It is completely domestic system. In this Bahis are used in recording of transactions in books of accounts. There are many different types of Bahiya such as Rokarbahi, Nakalbahi, Khatabahi etc. All transactions are written in local language so it is easily understandable. It is more accurate than Single Entry System. But in is computer era its scope is reduced. Generally medium level business man who has limited resources uses this system.

4) Basic Accounting Terminology

To understand any stream, it is necessary to understand basic terminology. So it is required to understand the basic accounting terms which are used in the Accounting. By this, accounting work becomes easy and simple. The main terminologies are....

Purchase

The term 'purchase' is used only for purchase of goods. If a business firm purchases and sells anything then those things which are purchased for resale are called 'Purchase'. If any firm produces something then purchase means purchase of raw materials because raw materials are converted into finished goods for sale. Important thing is that only those goods which are purchased for re-sale is called purchase. For example if a firm purchased a cloth material and then sells it, it is called purchase, but if it purchases furniture for office purpose which is not for sale, will not be called purchase. If he purchases cloth material to make trousers from it then sells, it also is called purchase and furniture for office will be called Asset. But if he does business of furniture then purchasing of furniture will be called 'purchase'.

Sales

The term 'sales' is used for sale of those goods which were purchased for resale. Selling of assets is not part of sale. The service which is provided by a person and receives income for it, is called sale. Sales include both cash and credit sales. If a businessman sells his office furniture, it is not called sale. Sales mean sales of trading. Here sale of machine is, sale of assets, not business sale.

Purchase Returns

Purchased goods may be returned due to any reason by businessman is called Purchase Return. It is also called Returned Outward. Here purchase means those goods which were purchased for resale. Similarly return of assets is also not purchase return.

Sales Returns

Sold goods when returned by the purchaser due to any reason are termed as sales return. This return is come into business again so it is called Return Inward also.

Capital

Capital means the amount which the proprietor has invested in business to start the business or expansion of business. Goods and assets are purchased by this amount. Goods are purchased for resale and assets are purchased for operation of business. Capital is internal liabilities of business. To calculate capital external liabilities are deducted from the assets.

$$\text{Capital} = \text{Assets} - \text{External Liabilities}$$

Capital is very important and necessary for business.

Drawing

It is the amount of money which the proprietor takes for his domestic or personal use. If proprietor withdraws goods from business for personal use it is also called Drawings. If the firm is a partnership firm then withdrawal of cash or goods by each partner for their personal use is called Drawings. Proprietor gives interest on drawings to business. In partnership firm the provision of interest may be in partnership deed and according to this, interest on drawings is given.

Assets

The proprietor has many resources in business ,like cash, bank balance, debtors, bills receivables, stock, furniture, machine, land and building etc. These will enable the firm to get cash or benefit in the future. These all have important role in a business. It is called assets.

According to R.N. Anthony “Assets are valuable resource owned by business which are acquired at a measurable money cost.”

According to this definition features of assets are.....

- 1) Resources should be valuable.
- 2) They are owned by business organisation.
- 3) They are measured by money value.

If the resources cannot be measured in money value, it is not asset. Assets enable the firm to get cash or benefit in the future.

Types of Assets

Assets can be classified as :

1) Fixed Assets

Fixed assets are those assets which are used in business for long time and purchase for the purpose of operating the business ,means production of goods and services. These assets are not for re-sale. Examples of fixed assets are land, building, plant & machinery, furniture, motor vehicles etc.

2) Current Assets

Current Assets are those assets of a business which are kept for re-sale or with a purpose to convert them into cash within an accounting year. These assets are called active or liquid assets also. It includes stock of goods, debtors, bills receivable, prepaid expenses etc. Bank balance and cash in hand are quick assets. Other names of current account are floating assets or circulating assets also, because they continually come and go into the business. Stock and short term investment are written in books of account at their cost value.

3) Intangible Assets

Assets can be classified in two parts : 1) Tangible Assets 2) Intangible Assets

The assets which can be seen in physical form are called Tangible Assets. Like building, land, machinery, stock, furniture etc.

Second by those assets which do not have any physical form and cannot be seen and touched are called intangible assets. For example goodwill, copyright, patents etc. These assets are also very important in business.

4) Fictitious Assets

The assets which do not have any physical existence, they are only on assumption base are called Fictitious Assets. Some times Goodwill shown in books without any value, is considered as Fictitious Assets. They don't have any importance. But when there is any loss in business then it is included in goodwill to increase value of goodwill.

5) Receivables

Receivables means receipts of business from debtors. For example when we sell goods to customer on credit, he becomes debtor of business, means firm claims money from him. So he may accept a bill which is payable after a given period. It is called Bills Receivable for a business firm. In other example when firm provides loan and advances to customer and the amount which is received after a particular time it is called Receivables.

It is shown in assets side of the Balance Sheet. In short, Debtor, Bills Receivables, Loan & Advances etc are receivables.

Liabilities

Receivables and receipts of the firm are considered as assets of business. Opposite of this the amount which has to be paid by the firm to persons and other firms are Liabilities of the firm. Liabilities means those amounts which are to be paid by the business to other persons and or firms. It is written in Liabilities side of the Balance Sheet.

Liabilities can be classified into the following.

1) External Liabilities

External Liabilities are the liabilities which are payable to outsiders. Long term loan, outstanding expenses, medium and short term loan, creditors, bills payable and legal taxes etc are external liabilities.

2) Internal Liabilities

The Liabilities which are to be paid to internal creditors after a long time period is called Internal Liabilities. Capital, Preference and equity share capital are mainly internal liabilities. The additional capital of the proprietor or partners, loan provided by partners are also called internal liabilities.

3) Short Term Liabilities

Basically it is also a part of liabilities which are mentioned above. These are liabilities which are payable in the near future (generally within a year). Creditors, bills payable, govt tax, outstanding expenses are short term liabilities.

4) Long Term Liabilities

Opposite of the short term liabilities, these are payable after a long time. Long term loan, debentures, capitals are these type of liabilities.

Some terminologies are given below which can help the students

- **Debtors**

A person who owns money to the firm generally on account of credit sale of goods is called Debtor. It is a current assets.

- **Bills Receivable**

The person who takes credit sales from business firm and after this he accept the bill for outstanding amount, that bill is called Bills Receivables . Debtor promises to pay the specific amount in specific period, which is mentioned in the bill. Bill can be discounted from bank before the due date if businessman feels requirement for money.

- **Creditors**

A person and or institution that the firm owes money on behalf of taking credit purchases are called Creditors.

- **Bills Payable**

The person and or institution, From whom firm takes credit loan or goods and business accepts bill to pay them on specific date it is called Bills Payable. They are accepted for certain period which is mentioned on the bill. The businessman has to pay the specific amount on due date.

Direct and Indirect Expense

Expenses are those amounts, which are to be paid for manufacture or sale of any goods and services. In this we include those expenses which are paid to start a business. The total paid amount for goods like purchase of raw material, wages, carriage expenses, rent of building, commission, salaries of employees, office rent advertisement, decrease in value of assets due to use of it etc. are called Expenses. If any business does not produce any goods and services then the payment related from purchase of goods or service to sell it is called Expenses.

Expenses are classified in two parts.

- **Direct Expenses**

The expenses which are directly related to any specific product and service are called Direct Expenses. In other words these expenses related to any specific product or service. For example purchase of raw material for a particular product, payment of wages for this product, expenses on electricity on that particular product etc are considered as Direct Expenses. But when two or more product are manufactured in a single building then rent of this building will not be direct expenses, because the rent is not paid for any particular product. It is for two or more products. So it is Indirect Expense. The expenses are considered in Direct Expenses when they are directly related to any particular product. An expense can be Direct Expense in a particular place but at the same time it may be indirect for other place. So decision of Direct and Indirect Expense will be

according to the situation.

- **Indirect Expenses**

If there is any expense (cash or non cash) which is not considered a direct expense, it is an Indirect Expense. So Indirect Expenses are those expenses which are not directly related to any particular or specific product. Generally they are related to more than one product. These expenses are divided into product and services on a particular basis. Basically these expenses are: salaries of employees, electricity expense of common area, salary of guards, commission for sale, advertising and distribution expenses, legal expenses, depreciation on machinery and plant, repair etc. Again any expense can be indirect or direct expense according to situations. So direct and indirect expenses are decided according to time, place, and situations.

Revenue Receipt and Capital Receipt

Revenue Receipts means the amount which are received by the business entity on regular basis from the operation of its business. For example, amount received from sale of goods and services, received rent, commission received, received interest on loan etc. are Revenue Receipts. They are received on regular basis on the operation of business.

Capital Receipts are those receipts, which are not in regular and recurring nature. They are received from sale of fixed assets, issue of share capital and debentures etc. Capital receipts are not directly related to regular operation of the business. The Capital Receipts are large in amount and received seldom.

Revenue Expenses and Capital Expenses

Just like receipts, Expenditures are also of two types: Revenue expense and Capital expense.

Revenue Expense helps the business in its operation, but does not increase the operational capacity of the business.

Capital expenses are large in amount but happen seldom. They increase the capacity of business. Revenue expenses are written in debit side of Profit & Loss account and Capital Expenses increase the fixed asset of business. Revenue Expenses are:- wages and salaries, office expenses, light and water expenses, advertisement and distribution expenses, etc. Capital Expenses are:- purchase of fixed assets, and installation of machinery resumption of debentures etc..

Deferred Revenue Expenditure

There are some revenue expenses, such as the benefit of those expenses is likely to be available to the firm over a period of several years. So these expenses are not to be written-off to a year's Profit & Loss Account. In fact they are to be written-off to several years in small-small amount. Like in 2015-16, ₹ 5 Lakh spent on advertisement, which will be benefited for next four years. So every year $\frac{1}{4}^{\text{th}}$ amount is to be written-off and remaining amount may be shown in assets side of Balance Sheet as a Deferred Revenue Expenditure.

Double Entry System

It is a very important system of Accountancy. It is a universal and reliable accounting system. As we all know, every business transaction has two aspects. One is called Debit and second is called Credit. In this system transactions are written to both aspects, so it is called Double Entry System. Although Accountancy is formed from ancient years but in systematic way, that is Double Entry System, was developed in 1494 when Lucas Pasiyoly wrote it in his book and presented it in front of the world. Now almost with the history of 500 years, it has been accepted as system of Accounting and broadly recognized. Double Entry System is absolutely different from Single Entry System. In this system, all business transactions are written in books of accounts. All transactions are written with proper principles and rules. It is systematic, complete, reliable, scientific and approved accounting system in the field of accounting.

The significances of Double Entry System are:

- All transactions are written in both aspects in books of accounts. One is Debit and other is Credit.
- In this system all types of accounts can be opened and written like Personal accounts, Real accounts and Nominal accounts.
- All business transactions are written fully and mathematical accuracy can be checked by Trail Balance.
- After making Trail Balance, profit or loss can be calculated for the year ending. So Trading and Profit & Loss Account are made. And after the end of accounting year to know the financial position of business Balance Sheet is prepared. These are all included in final accounts.
- All required adjustments are done at the time of Final Accounts.
- This system is universally accepted and reliable accounting system.
- This system is useful in all types of business organisations (small, medium or big) and purely scientific method. Generally it is written in English Language.
- In present computer era, use of computer is increasing in this system day by day. So accounting work becomes faster, accurate, economic and fast communicative by the use of computer.
- Generally in this system there are 3 types of accounting books: Journal. Ledger and Cash book. As per the requirements and number of transactions some subsidiary books are also to be maintained, like Purchase Book, Sales Book, Purchase Return book, Sales Return Book, Petty Cash Book etc.

Principles/Rules of Double Entry System

In this system business transactions are written on the basis of some specific principles. The rules are:

- ❖ For Personal Account: Debit the account of receiver and credit the giver.

- ❖ For Real Account: Debit the account of what comes in and credit what goes out.
- ❖ For Nominal Account: Debit the account of all expenses and losses and credit all incomes and profits.

Firstly decide both aspects of account from transactions and then debit or credit them according to rules or principles.

Basic Accounting Concepts, Assumptions and Conventions:

Accounting system's theory is based on its concepts, assumptions, rules and conventions. Without knowledge of basic principles of any subject it is hard to understand it. In present time Accountancy is the important activity of business ,because many persons like owner, shareholders, creditors, investors, government, society, customer etc are interested in the financial statements and they are benefited from it. So it is necessary that Accounting should be written in such a language so that it can be useful for all and can be understood in proper way, and can compared easily. So we should use some specific concepts, assumptions and conventions in Accounting.

A) Accounting Concepts and Assumptions:-

Generally concepts and assumptions are same. Some important concepts and assumptions are discussed below. Without this Accounting cannot be written properly.

❖ Business Entity Concept

The Business Entity Concepts describe that business and owner of business are two separate entities. It is applicable for all type of business organisations. So that capital of proprietor is a liability of the firm and owner is considered as a creditor of the firm. Whenever the business will windup then capital is to be returned to proprietor. This concept separates the business from its owner. It is a very important concept. Due to this reason business man's personal assets, liabilities etc are not written in accounting books.

❖ Money Measurement Concept

According to Money Measurement Concept, the transactions and events that can be measured in terms of money are only recorded in the books of accounts of the firm. Although Accountant is very effective and honest but the ability and honesty can-not be measured in money terms, so it is not the matter of accounting. This is an important concept because of this in all business organisations only those transactions which have money value are recorded in the books of accounts. Remember that only monetary measurement is the base of addition of transactions and to be written in books of accounts. In a business there are 10 air conditioners but cannot have money value then it cannot be written in books of accounts. Money measurement is easy to understand.

❖ Going Concern Concept

The Going Concern Concept means a business shall continue for long time period. Although

decision of definite period is not possible but it is expected that it will continue for a long time period. On the basis of this concept, fixed assets are recorded after the deduction of depreciation from its original cost, not by market cost. According to this concept, any external person gives goods, services or money on credit. Classification of assets and liabilities are also based on this concept, otherwise it is a difficult task.

Accounting Period Concept

It is true that, business will continue for a long time period. But for financial results of business transactions and for fair financial position of the firm accounts are prepared on a regular interval. A number of users are excited and eager to know the financial results or statements. For the comparison, analysis (one firm to another firm although both have same business) all business organisations adopt accounting year (01 April to 31 March). According to this concept, financial year which is Accounting Year, Trading and Profit & Loss Account are prepared at the end of this period. So that profit or loss can be calculated and financial position can be measured.

❖ **Cost Concept**

According to the Cost Concept, an asset is recorded in the books of accounts at the price which has been paid to acquire it. Depreciation is deducted from the purchase price then it is shown in balance-sheet. This will continue in further years so that books of accounts can be prepared systematically. Assets are shown at their cost value less depreciation so it is also called Historical Cost Concept. Although the market value of assets are changed but generally acquire cost is shown. It does not mean that it will always remain the same. After some time or whenever required original value can be calculated. But it has some difficulties. Market value always changed. Sometimes assets become out dated. The Cost Concept is also matched with the Going Concern Concept. Business will be continued for long time so assets should be valued on the basis of Cost Concept.

❖ **Dual Aspects Concept**

According to this concept each business transaction which is written in books of accounts, affects two sides or two accounts. If one side is debited then other side will be credited. This concept is applicable on Double Entry System. For example purchased goods on credit ₹ 50,000, then according to rule Purchase Account is to be debited and Cash Account is to be credited. So that total of both sides will be equal. If there is any change in one side then other side will also be changed.

❖ **Revenue Realisation or Recognition Concept**

The Revenue Recognition Concept means revenue is considered to have been realised, when the transaction has been entered into books of accounts and amount has been received. According to R.N. Anthony “Revenue is considered as being earned on the date at which it is realised, that is, the date when goods or services are produced to the customers in exchange for cash or for other valuable consideration.”

Generally in business, revenue reorganisation is considered on sale. As the goods or services are received by customers the selling process is completed. But the professional service providers consider revenue, when cash is received. In contract work revenue realisation is taken into consideration on the basis of ratio of contract cost.

❖ **Matching Concept**

It is also an important concept, according to this concept when the revenue is considered; expenses are also considered at the same time. Means when and that type of revenue is written in books of accounts, expenses should also be written in same manner. So, because of this concept, outstanding expense, prepaid expenses, accrued income are adjusted in final accounts and stock of business on last date of accounting year is treated as opening stock of next year. And adjustment of accrued income or income due but not received are made.

This concept is also called Accrual Concept. According to Accrual Concept a transaction is recorded at the time when it takes place and not when the settlement takes place. Similarly the expenses are recorded in books at the time when the revenue received from it, not when the cash is paid.

❖ **Objectivity Concept**

This concept emphasise on that the business transactions should be written in a definite system in books of accounts. It should be free from personal bias. This concept may be based on the accountant or the manager but should be reliable facts. For example, sold goods in cash and received cheque; so it should be checked by proper bill and cheque.

B) Accounting Conventions:-

Accounting Conventions can be understood as mutual acceptance of accountants. They are not based on legal aspects. These are traditional rules which are followed on mutual acceptance.

These are not in Accounting Principles. Accounting Principles are based on rules, laws and bias free. But Accounting Conventions are not like that. These are normally traditions of business field. Some main conventions are as follow :

❖ **Conventions of Consistency**

The Conventions of Consistency shows that accounting rules and practices once selected and adopted, should be applied year after year in the same manner. It should not be changed every year. So the comparison becomes easier of profit or loss for the year, financial results for managers and other users. If the rules and practices are changed every year then it will be difficult to calculate profit or loss of year. Generally it is not changed in every year.

But what this 'conventions' means is not that we never change the rules and practices of accounting. There can be change in Accounting Principles according to situations. By this, Accounting system can be flexible, otherwise it will be rigid. The change can be beneficial for better results, presentations and information.

❖ **Conventions of Full Disclosure**

This convention shows that all important financial information should be disclosed. This convention is very popular, now a days financial results and information are used by many persons and institutions to take decisions.

There are many provisions in Company Act 2013 regarding disclosure of information. Development of Information technology makes this work more easy, quick and less expensive. There are many provisions in Company Act regarding Profit and Loss account and Financial Statement so that comparison of units can be done. The information which is not mentioned in Profit & Loss Account or Balance Sheet is shown in Notes of Accounts or Footnotes. For example doubtful assets, change in methods of valuation of assets and stocks, market value of investments etc.

❖ **Conventions of Conservatism**

It is also called conventions of conscious. According to this Profit is not considered as profit whenever it is not to be received. But if there is any loss or probability of loss then it should be mention in books of accounts. It shows the consciousness of business which develop the faith of investors. So all expected losses are shown in books of accounts, but expected profits are not written in books.

According to this concept if there are many methods to write any transaction then the alternative which has less impact on profit, should be selected. This is the reason that market price or purchase price whichever is less should be selected and shown in books of accounts. In other example provision of bad debts, group insurance, etc. because of this conventions, Profit & Loss Account shows less profit and loss in comparison to real profit or loss. And in Balance Sheet, assets are shown on less value and liabilities are shown comparatively on high value. It is a disadvantage, but it is right for business or investor's point of view.

❖ **Convention of Materiality**

Materiality means the important information or facts which can be effect the decision of users. Sometimes from business point of view these information should not be disclosed. They are disclosed indirectly or with the other information. This concept is opposite of Convention of Disclosure. According to American Accountancy Commission an item should be regarded as material if there is any reason to believe that knowledge of it would influence decision of informed persons. Materiality item can be different from one organisation to another or one person to another. In this, nature of transaction, cash etc. are important. For a normal person ₹500 for repair may be important but for a big businessman or organisation it may not be important. This is the decision of Accountant that the information is material or not.

Important Points

- Accountancy is a whole process of Accounting.
- Book-keeping is the base of Accounting and the first step of Accountancy.

- Book-keeping means writing the business transactions in books of accounts.
- Those transactions are written in books of accounts which can be measured in money value.
- In Book-keeping, transactions are identified, recorded in primary books and classifying them and posting them into in Ledger.
- When the work of Book-keeping completes, the work of Accounting starts.
- In accounting, from the classified transactions, profit or loss is calculated on yearly basis.
- On a specific time (last day of accounting year) to know financial position of business, Balance Sheet is prepared.
- There are many sub-divisions of Accounting. The main are, Financial Accounting , Cost Accounting, Management Accounting, Social Accounting etc.
- Accountancy has close relation with other subjects like Maths, Statistics, Economics, Sociology, Law.
- In Accountancy there are three types of system: Single Entry System, Double Entry System and Indian Accounting System.
- Single Entry System is incomplete. Indian Accounting System is popular at local level in India and Double Entry System is universally adopted.
- For doing the work in Accountancy, to the knowledge of basic principles, concepts and conventions is essential .

Questions for Exercise

(A) Very Short Answer Questions

- What do you mean by Book-keeping?
- What is done in Accounting?
- What are the two main objectives of Accounting?
- What type of business transactions are written in Accounting?
- "5 computers are in business organisation." How will it be written in Accounting?
- "Sales manager is very efficient and honest person". Write this in Accounting?
- Is Accounting an Art?
- Why Accounting is called Science?
- Write the name of Accounting Systems?

- What is Drawings?
- Give the example of short term liabilities.
- What is the rule of Personal Account to record in books

B) Short Answer Questions

- What types of Accounting Books are used in Book-keeping?
- Describe the Book-keeping?
- What is the main work of accounting ? Describe.
- What are the names of subjects, which are related to Accounting?
- What is the sub-division of Accounting?
- What is Indian Accounting System?
- What do you mean by Business Liabilities?
- Give the 3 examples of Intangible Assets?
- What is the meaning of Fixed Assets? Give 2 examples.
- What do you understand by Double Entry System?
- Describe any two conventions of Accounting?
- Give the name of any 3 concepts of Accounting?
- Who are the users of accounting information?
- What are the rules of Accounting (for different types of accounts)?

C) Long Answer Questions

- "Where work of Book-keeping completes, work of Accounting starts". Describe this statement.
- What do you mean by Accounting? Describe Book-keeping and Accounting both.
- Describe briefly sub-division of Accounting.
- With the limitations of Single Entry System describe it briefly.
- Describe any 5 terms of accounting terminology.
- What are the differences in Single Entry System and Double Entry System?
- Describe the main concepts of accounting.

Key Words

Book Keeping

Financial Accounting

Cost Accounting

Managerial Accounting

Social Accounting

Statistics

Management

Single Entry Accounting System

Double Entry Accounting System

Mahajani System of Accountancy

Purchase

Sales

Purchase Return

Sales Return

Capital

Drawings

Assets

Fixed Assets

Current Assets

Factionous Assets

Intangible Assets

Receivables

Liabilities

External Liabilities

Internal Liabilities

Short Term Liabilities

Long Term Liabilities

Debtors

Bills Receivables
Creditors
Bills Payable
Direct Expenses
Indirect Expenses
Revenue Receipts
Capital Receipts
Debits
Credits
Personal Account
Real Account
Nominal Account
Concepts
Conventions
Business Entity Concept
Money Measurement Concept
Going Concern Concept
Accounting Period Concept
Cost Concept
Revenue Recognition Concept
Matching Concept
Objectivity Concept
Convention of Consistence
Conventions of full Disclosures
Conventions of Conservatism
Conventions of Materiality