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FINANCIAL ACCOUNTING SEMESTER – I
B.COM. – I SHORT NOTES

1. Objectives of Accounting:

i) To keep a systematic and permanent record of all the transactions.
ii) To keep the record of incomes and expenses.
iii) To keep the record of assets and liabilities
iv) To evaluate earning capacity of the firm.
v) To control on expenses to minimise the expenses.
vi) To help in decision making.
vii) To provide accounting information.
viii) To fulfil legal requirement.

2. Branches of Accounting:

i) Financial Accounting:

Financial Accounting is recording of the financial transactions to find out trading results and financial position at the end of the year.

ii) Management Accounting:

Management Accounting helps the management to perform all its functions.

iii) Cost Accounting:

Cost Accounting is a set of procedure for determining the cost of a product.

iv) Social Responsibility Accounting:

Social Responsibility Accounting is the measurement and reporting, internal and external, of information concerning the impact of Entity and its activities on society.

3. Business Entity Concept:

This concept implies that a business unit is separate and distinct from the persons who are owners of the business. A limited company is an artificial person created by law and thus it has a separate legal entity from its owners i.e. shareholders. The accounting equation 'Assets = liabilities + capital' is an expression of the entity concept.

4. Going Concern Concept:

According to this concept it is always presumed that the business is having a perpetual succession. A limited company being an artificial person created by law, it has uninterrupted existence with continuing activity till such time it is legally liquidated.

5. Dual Aspect Concept:

This is the basic concept of accounting. According to this concept every business transaction has a dual i.e. two-fold effect i.e. every debit has a corresponding credit. The entire double entry system is based on this concept.

6. Conservatism Convention:

On account of past bad experience, the accountants agreed to follow the rule 'anticipate no profit but provide for all possible losses' while recording business transactions. On this basis the stock is valued at cost or market price whichever is lower. Similarly, provision is made for possible doubtful debts.

7. Consistency Convention:

According to this convention, the policy once adopted should not generally be changed- it should be consistently followed from one period to another e,g. policy followed in respect of valuation of closing stock. Similarly there are different methods of depreciation.

8. Accounting Standard -2 (AS-2): Valuation of Inventories :

According to Accounting standard inventories should be valued at lower of historical cost and net realisable value. For the purpose of comparing historical cost with net realisable value each item in the inventory may be dealt with separately, or similar items may be dealt with as a group. The historical cost of manufactured inventories may be arrived at on the basis of either direct costing or absorption coating.

9. Accounting Standard -6 (AS-6): Depreciation Accounting:

The amount of depreciation on an asset should allocated to each accounting period during the useful life of the asset. The method of depreciation selected should be applied consistently from period to period. The useful life of a depreciable asset should be estimated. Depreciable asset may be reviewed periodical. The provision for depreciation should be based on revalue amount.

10. Accounting Standard -10 (AS-10): Accounting for Fixed Asset :

Fixed asset is an asset held with the intention of being used for the purpose of producing or providing goods and services and is not held for sale. The gross book value of a fixed asset should be either historical cost or a revaluation cost. The cost of a fixed asset should comprise its purchase price and any attributable costs of brining the asset to its working condition for its intended use. Gross and net book value of fixed assets at the beginning and end of an accounting period are showing additions and other movements.

11. Amalgamation of Partnership Firms:

The firms carrying on similar businesses agree to end their separate existence, combine their businesses and form a new firm. Thus merging of two or three separate firms into a new single firm is called the amalgamation of firms. As the old firms are required to be closed for this purpose each of the old firms is required to take the following steps;

i) To revalue the assets and liabilities as agreed by the new firm. The profit or loss on revaluation A/c is transferred to partner's capital account.
ii) Goodwill A/c is raised in the books of accounts.
iii) The assets and liabilities of the old firms are transferred to the new firm at agreed values.
iv) The final balances on the capital accounts are transferred to the new firm.

12. Treatment of Goodwill in Amalgamation:

i) If Goodwill A/c is to be maintained at full value, no separate entry is required to be passed in the books of accounts.

ii) If Goodwill A/c is not to be maintained in the books of the new firm capital accounts of all the partners are to be debited and Goodwill A/c is to be credited.

iii) If only some amount is to be written off capital accounts are to be debited and Goodwill A/c is to be credited with the amount to be written off.

13. Adjustment of capitals in new firm in Amalgamation:

It may be agreed to maintain certain amount of the total capital of the new firm. The balances of capitals transferred to the new firm or the balances remaining on capitals after writing off. The capitals desired may therefore be maintained either by bringing or paying cash or by adjusting the amounts through the current accounts.

If the capital balances are less than the desired amounts, the partners may bring cash or current accounts may be debited and capital accounts are credited.

If the capital balances are more than the desired amounts the partners capital accounts are debited and cash or current accounts may be credited.

14. Consignment:

Consignment is a dispatch of Goods by the Consignor to Consignee for sale for sale on commission basis, on the risk and account of the consignor; it is not a sale by the consignor or a purchase by the consignee. As such the ownership in the goods dispatched does not pass over to the consignee. The ownership of the goods remains with the consigner and the sale proceeds belong to the consignor. In consignment, the sender of goods is called a consigner and the person to whom the goods are sent is called a consignee. Thus, the relation between the consignor and the consignee is that of principal and agent.

15. Proforma Invoice:

A consignor prepares a 'Proforma Invoice' at the time of dispatching goods to consignee and sends it to the consignee along with the goods. It gives full particulars of the goods consigned, such as the value of goods, the means of transport, the expenses paid by the consignor etc. Hence, the invoice is sent to consignee by way of information only and as such it is called a 'Proforma Invoice'.

16. Account Sales:

The consignee is agent of the consignor. At periodical intervals the consignee submits a statement, known as Account Sales, giving the details regarding sales made, expenses paid by him, his commission, the amount paid by him and the balance due to the consignor etc.

17. Commission:

The consignee is a commission agent of the consignor and as such the consignee is entitled to receive commission on the goods sold by him as per agreement. Besides the sales commission at an agreed percentage on the gross sale proceeds. Simple commission, Del Credere commission and special commission these are the different types of commissions may be received by the consignee.

18. Del - Credere commission:

This commission is allowed to the consignee to bear the loss of bad debts, if any, arising out of credit sales effected by the consignee. In the absence of this commission the loss of bad debts is required to be borne by the consignor. This commission is calculated on total sales, unless it is specifically agreed to calculate it on credit sales only.

19. Special Commission:

In order to induce the consignee to sell the goods at the maximum possible price special commission is given. This commission is given on the sale proceeds exceeding the invoice price of the gross sold. The consignee is to get commission at agreed percentage on extra sales price in addition to the normal commission.

20. Valuation of Closing Stock / Consignment Stock:

In order to arrive at the profit or loss on consignment, it is necessary to value unsold goods i.e. stock lying with the consignee. The general principle that the stock is to be valued at 'cost or market price whichever is lower' is followed here also. But here cost does not mean only the original purchase price but it means the original price plus proportionate amount of expenses incurred by the consignor and proportionate amount of non-recurring expenses such as freight, carriage, clearing charges, customs duty, dock dues, loading and unloading charges etc. incurred by consignee.

21. Normal Loss:

The loss which is inherent and which cannot be avoided is termed as normal loss. The nature of goods is such that in packing and handling the goods e.g. coal and sprit. In loading and unloading the coal, some quantity is bound to turn into dust. Similarly, in the case of sprit, some loss is bound to occur due to evaporation. The unsold goods lying with the consignee are valued at enhanced rate, deducting the normal loss from the quantity of goods sent on consignment.

22. Abnormal Loss:

It is not a natural loss and it can be avoided if due care or precaution is taken. Such loss may arise due to accident, theft, carelessness etc. It is the general principle that such loss should not affect the consignment profit or loss. The valuation of the goods lost is done on the lines of valuation of closing stock i.e. original cost of the goods lost plus proportionate amount of expenses incurred by the consignor.

23. Receipts and Expenditure Account:

Professional persons prepare Receipts and Expenditure Account to ascertain profit or loss of their professional activities. In this account mercantile system is followed in respect of expenses only i.e. both cash payments as well as outstanding expenses relating to that particular period are recorded. However, cash system is followed in respect of items of incomes such as fees, other charges etc. Outstanding incomes are not taken into account.

This account is prepared as income and expenditure A/c, but the only difference is the current year outstanding incomes are debited to Receipts and Expenditure Account as "provision for outstanding incomes" and last year outstanding incomes are credited to Receipts and Expenditure Account.

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