Financial Accounting 1
Chapter:- Introduction to Accounting
B.COM (SEM:-I)

Presented By,

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Financial Accounting 1

- ✓ **UNIT 1: INTRODUCTION (5 MARKS)**
- ✓ **UNIT 2: CONCEPT FOR DETERMINATION OF BUSINESS INCOME (15 MARKS)**
- ✓ **UNIT 3: INTRODUCTION TO ACCOUNTING STANDARDS (10 MARKS)**
- ✓ **UNIT 4: FINAL ACCOUNTS OF TRADING CONCERN (15 MARKS)**
- ✓ **UNIT 5: FINANCIAL STATEMENT FROM INCOMPLETE RECORDS AND OF NPO (10 MARKS)**
- ✓ **UNIT 6: ACCOUNTING FOR SPECIAL SALES TRANSACTION (25 MARKS)**

Chapter:- Introduction to Accounting

NATURE OF ACCOUNTING

- ✓ Man made system
- ✓ Accounting is a process
- ✓ Accounting is an art
- ✓ Monetary events
- ✓ Accounting is a means and not an end

- ✓ a) Faithful representation
- ✓ b) Neutrality
- ✓ c) Prudence
- ✓ d) completeness

Recording and classification of transaction

Reflecting the financial results

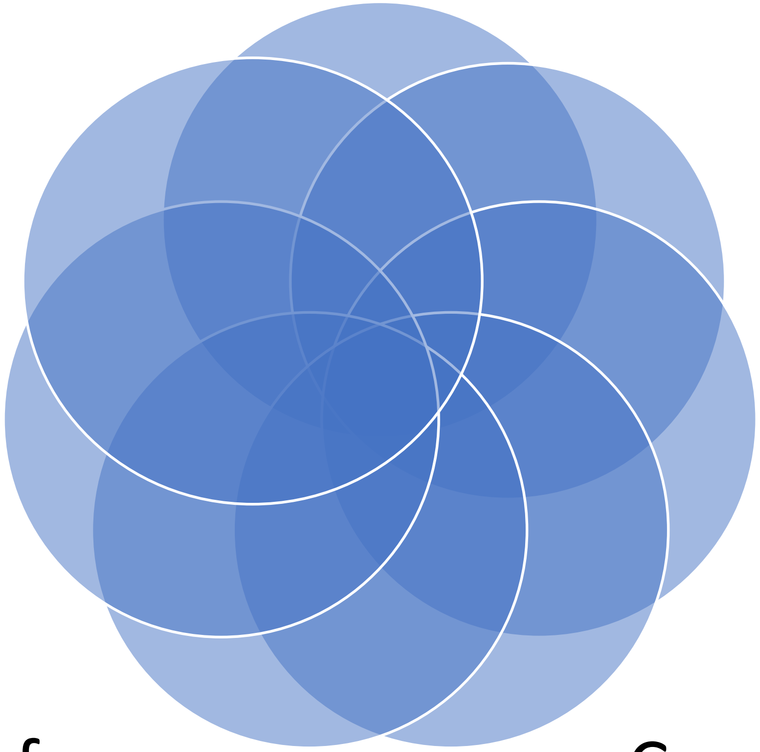
Reflecting the financial position

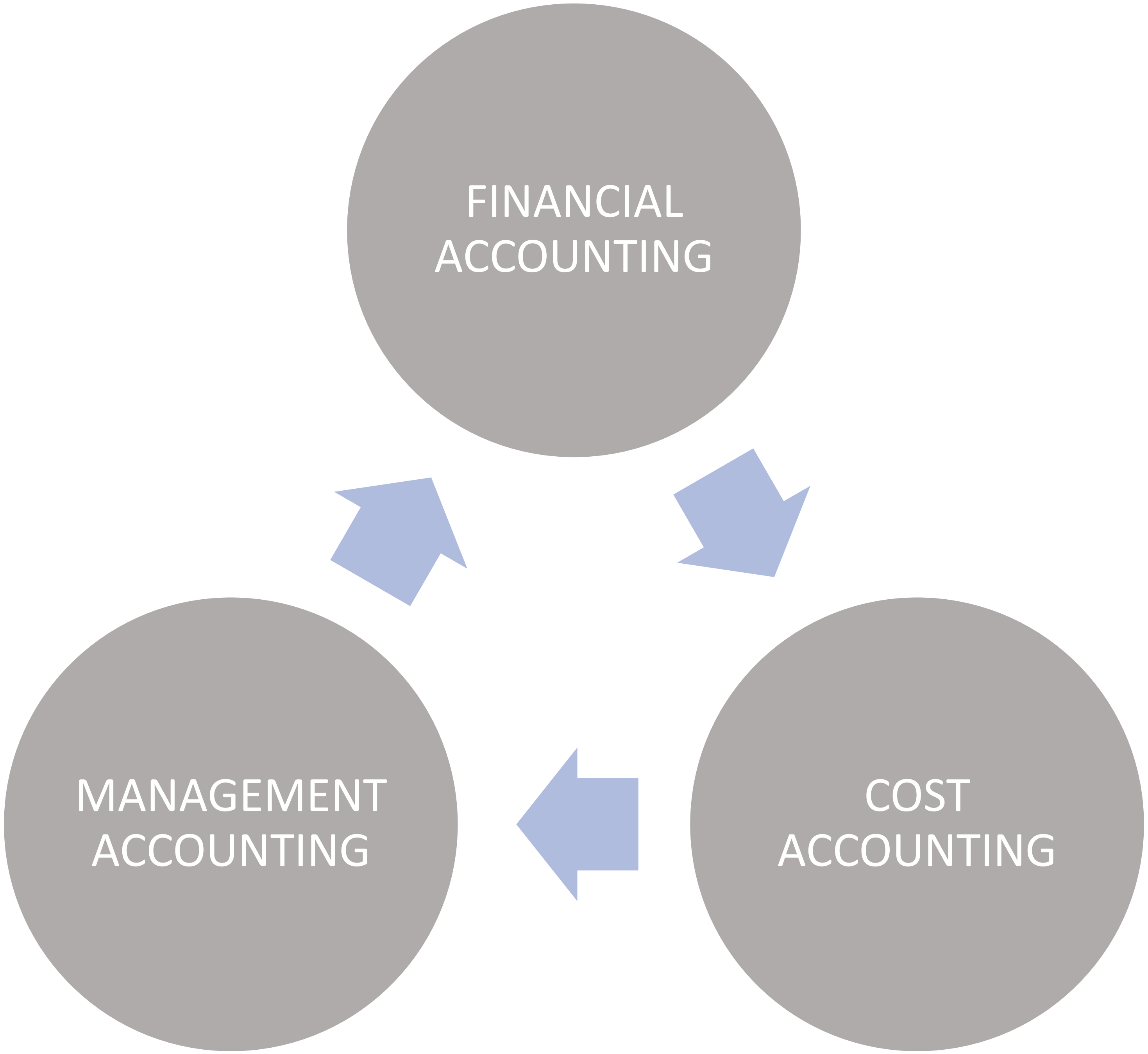
Communicating financial information

Sorting of economic events

Protection of capital

Best utilisation of available resources




FINANCIAL ACCOUNTING
COST ACCOUNTING
MANAGEMENT ACCOUNTING

BASIS FOR COMPARISON	FINANCIAL ACCOUNTING	MANAGEMENT ACCOUNTING
Meaning	Financial Accounting is an accounting system that focuses on the preparation of a financial statement of an organization to provide financial information to the interested parties.	The accounting system which provides relevant information to the managers to make policies, plans and strategies for running the business effectively is known as Management Accounting.
Orientation	Historical	Future
Users	Both internal and external users	Only internal users
Nature of statements prepared	General-purpose financial statements	Special purpose financial statements
Rules	Rules of GAAP are followed	No fixed rules for the preparation of reports
Reports	Only financial aspects	Both financial and non-financial aspects
Time Span	Financial statements are prepared for a fixed period, i.e. one year.	Management Reports are prepared whenever needed.
Objective	To create periodical reports	To assist internal management in planning and decision-making process by providing detailed information on various matters.
Publishing and auditing	Required to be published and audited by statutory auditors	It is not meant to be published or audited. It is for internal use only.
Format	Specified	Not Specified

<u>INTERNAL USERS</u> → Proprietor / shareholder/ partner | Management | Employees

<u>EXTERNAL USERS</u> → Investors | Lenders | Suppliers | Customers | Government

- ✓ The primary object of accounting is to provide necessary information to the owners/shareholders related to their business.

- ✓ The managers of business houses are more concerned with the accounting information because they are responsible to the owners.

- ✓ Employees are also interested in financial statements because an increase in their salaries, incentives, and wages and payment of bonus depends on the size of the profit earned.

- ✓ The persons who are interested to make an investment in business will like to know about its profitability and financial position. Thus, they derive this information from the accounting reports of the business.

- ✓ lending institutions would like to be ensured that they will be paid on time. Moreover, the financial reports help them in judging such position. Thus, Banks and other lending agencies rely upon accounting statements for determining the acceptability of a loan application.

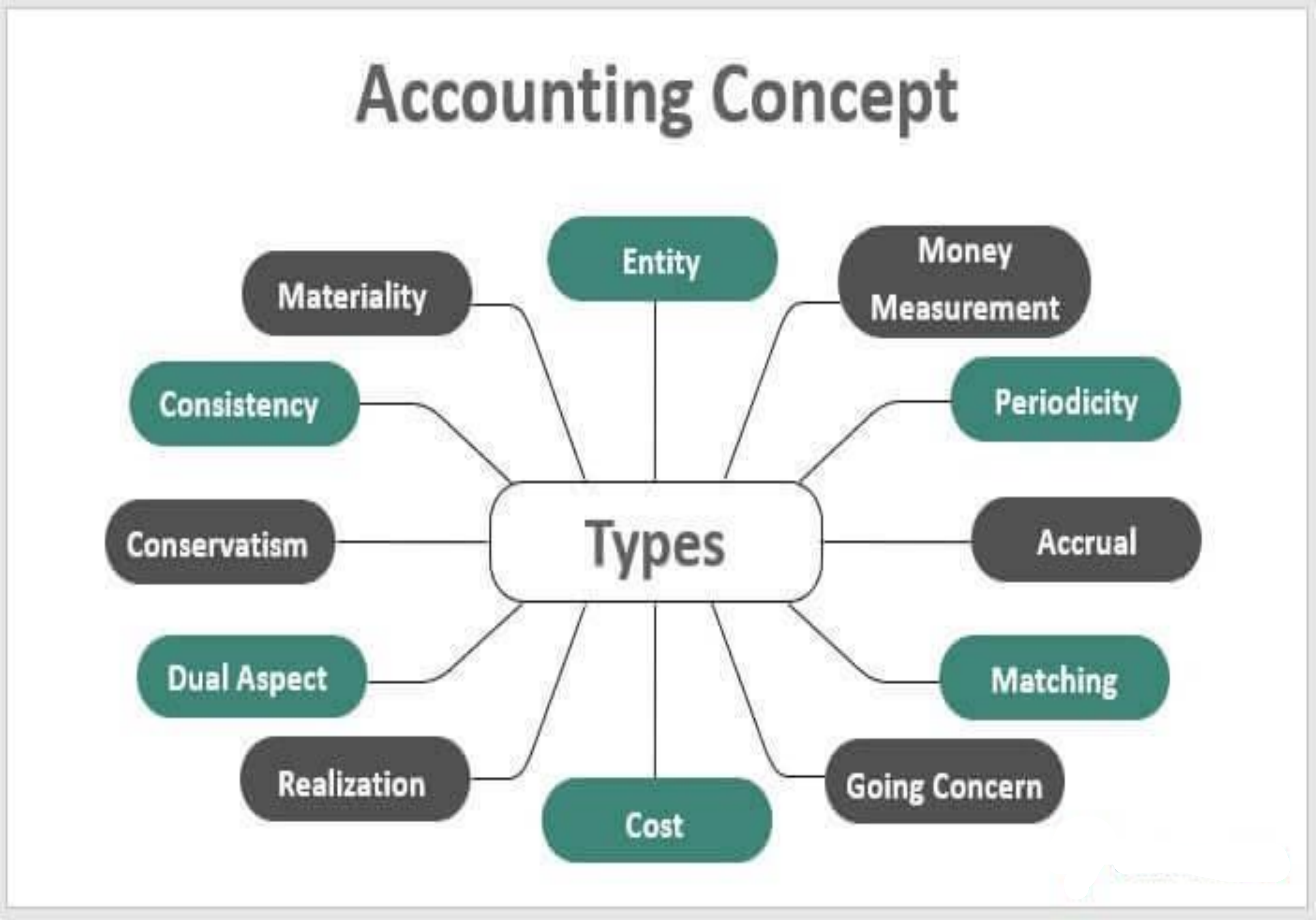
- ✓ Customers may also have either a short-term or long-term interest in the business entity to know the profitability, liquidity and solvency position of the business.

- ✓ The Government is interested in the financial statements of business organization on account of taxation, labour, and corporate laws.

- ✓ Accounting information is also used by the research scholars in their research in accounting theory as well as business affairs and practices.

- ✓ Various Government agencies and departments like Registrar of Companies, Company Law Board and Tax Authorities, etc. use accounting information.

- ✓ They not only require it as a basis for tax assessment but also in evaluating how well various businesses are operating under law related requirements.


Accounting Concept
Types
Entity
Money Measurement
Periodicity
Accrual
Matching
Going Concern
Cost
Realization
Dual Aspect
Conservatism
Consistency
Materiality

Basic Accounting Concepts

1] Business Entity Concept

This accounting concept separates the business from its owner. As far as accounting is concerned the owner and the business are two separate entities. This will help the accountant identify the business transactions from the personal ones. All forms of business organizations (proprietorship, partnership, company, AOP, etc) must follow this assumption.

So for example, if the owner brings in additional capital into the business, we will treat this as a liability on the balance sheet of the business.

2] Money Measurement Concept

This accounting concept states that only financial transactions will find a place in accounting. So only those business activities that can be expressed in monetary terms will be recorded in accounting. Any other transaction, no matter how significant, will not find a place in the financial accounts.

3] Going Concern Concept

The going concern concept assumes that a business will continue to operate indefinitely. So it assumes that for the foreseeable future the business will not be winding up. This leads to the assumption that the business will not have to sell its assets any time soon and it will meet all its obligations as well.

4] Accounting Period Concept

Every organization, according to its needs, chooses a specific period of time to complete an accounting cycle. Generally, the time chosen is a year we call the accounting year. The time period is mentioned in the financial statements.

5] Cost Concept

This accounting concept states that all assets of the firm are entered into the books of account at their purchase price (cost of acquisition + transport + installation etc). In the subsequent years to, the price remains the same (minus depreciation charged). The market price of the asset is not taken into consideration.

6] Dual Aspect Concept

This concept is the basic principle of accounting, it is the heart and soul. It basically is one of the golden rules of accounting – for every credit, there must be a corresponding debit. So every transaction we record must have a two-fold effect, i.e. it will be recorded in two places. This is the core concept of the double-entry system of accounting.

7] Realisation Concept

According to the realization accounting concept, revenue is only recognized when it is realized. Now revenue is the cash inflow for a business arising from the sale of goods or services. And we assume this revenue as realized only when it legally arises to be received. So in simpler terms, the profit earned will be recorded when it is actually earned.

8] Matching Concept

This concept states that the revenue and the expenses of a transaction should be included in the same accounting period. So to determine the income of a period all the revenues and expenses (whether paid or not) must be included.

9] Full Disclosure Concept

This concept states that all relevant information will be disclosed in the accounting statements. A lot of external users depend on these financial statements for their information to make investing decisions. So no information/transactions etc of relevance to anyone of them will be omitted from these statements for the benefit of the company.

10] Consistency Concept

Once the company decides on a certain accounting policy it should not be frequently changed. Unless there is a statutory requirement or it allows better representation of the accounts accounting policies should be consistent for long periods of time. This allows users to make inter-firm and inter-period comparisons. Also, frequent changes in policies may be to manipulate the accounts and this must be prevented.

11] Conservatism Concept

This accounting concept promotes prudence in accounting. It states that profit should not be included until it is realized. However, losses even those not realized but with the remote possibility of occurring should be included in the financial statements. So all losses are recognized – those that have occurred or are even likely to occur. But only realized profits are recognized.

12] Materiality Concept

Materiality states that all material facts must be a part of the accounting process. But immaterial facts, i.e. insignificant information should be left out. The materiality of a transaction will depend on its nature, value and its significance to the external user. If the information can affect a person’s investing decision then it is definitely a material fact.

Accounting conventions were established with a motive to bring uniformity in the books of accounts at the time of preparing them. Conventions are like customs/traditions that help the accountant to communicate clear accounting picture. In other words, accounting convention sets the guideline for the accountant that in turn helps him/her to prepare accounting statements and reports.

4 Major Accounting Conventions

- ✓Conservatism Convention
- ✓Consistency Convention
- ✓Accounting Convention of Materiality
- ✓Convention of Full Disclosure

Conservatism Convention

As per the Conservatism convention at the time of recording any financial transaction, you should recognize no profit but provide for all possible losses. This is the most important convention as it depends upon the theory that the future is uncertain. For instance, the value of inventory is recorded at cost or market price whichever is less. In a similar way, the provision for doubtful debts is also created. However, conservatism impacts current assets and liabilities.

Convention of Full Disclosure

Full disclosure convention helps the user in the proper interpretation of the financial statements of the company. As per this convention at the time of preparing records, full disclosure of financial information shall be made by the accountant.

Full disclosure can be made in two ways:-

- Either in the body of the financial statements, or
- In notes accompanying such financial statements

Consistency Convention

According to the convention of consistency once the company has decided to follow a method of accounting then it shall consistently follow the same method throughout. Along with this, changing the accounting method often would make the comparison of its own financial statements of different period difficult for the company.

Accounting Convention of Materiality

As per the accounting convention of materiality, an item is material if it can influence the decision of users of the financial statements. This convention is related to the significant importance of any event or item. Moreover, the materiality of an item depends on its amount and an events materiality depends upon its nature.

GAAP (Generally Accepted Accounting Principles)

Generally Accepted Accounting Principles (GAAP) are basic accounting principles and guidelines which provide the framework for more detailed and comprehensive accounting rules, standards and other industry-specific accounting practices. For example, the Financial Accounting Standards Board (FASB) uses these principles as a base to frame their own accounting standards. Thus GAAP encompasses:

GAAP encompasses:-

✓Basic accounting principles/guidelines

✓Accounting Standards usually issued by the premier accounting body of the country

✓Industry-specific accounting practices to cover unusual scenarios

✓**Principle of consistency:** This principle ensures that consistent standards are followed in financial reporting from period to period.

✓**Principle of permanent methods:** Closely related to the previous principle is that of consistent procedures and practices being applied in accounting and financial reporting to allow comparison.

✓**Principle of non-compensation**: This principle states that all aspects of an organization's performance, whether positive or negative, are to be reported. In other words, it should not compensate (offset) a debt with an asset.

✓**Principle of prudence**: All reporting of financial data is to be factual, reasonable, and not speculative.

✓**Principle of regularity**: This principle means that all accountants are to consistently abide by the GAAP.

✓**Principle of sincerity**: Accountants should perform and report with basic honesty and accuracy.

✓**Principle of good faith**: Similar to the previous principle, this principle asserts that anyone involved in financial reporting is expected to be acting honestly and in good faith.

✓**Principle of materiality**: All financial reporting should clearly disclose the organization’s genuine financial position.

✓**Principle of continuity**: This principle states that all asset valuations in financial reporting are based on the assumption that the business or other entity will continue to operate going forward.

✓**Principle of periodicity**: This principle refers to entities abiding by commonly accepted financial reporting periods, such as quarterly or annually.


ACCOUNTING
STANDARDS

- ✓ Accounting Standards can be any form of statement which consists of rules and guidelines, issued by the accounting institutions, for the preparation of uniform and consistent financial statements. This also includes disclosures required by the different users of accounting information.

- ✓ Accounting Standards (AS **1- AS 32**) have been issued by the Accounting Standards Board of ICAI, to establish uniform standards for preparation of financial statements, in accordance with the Indian GAAP (Generally Accepted Accounting Practices), for better understanding of the users.

- ✓ Accounting standards ensure the financial statements from multiple companies are comparable. Because all entities follow the same rules, accounting standards make the financial statements credible and allow for more economic decisions based on accurate and consistent information.

Importance of Accounting Standards

- ✓ Brings uniformity in Accounting system
- ✓ Easy comparability of financial statements
- ✓ Assist auditors
- ✓ Avoid fraud & manipulation
- ✓ Provide reliability to financial statement
- ✓ Make Accounting information easy & simple
- ✓ Measure management performance

IFRS

International Financial Reporting Standards

- ✓ Consistent preparation of financial statements by different firms & different industries has been assured leading to the possibility of inter firm & inter industry comparison of affairs.

- ✓ Helps accountant and auditors by providing the guidelines prepared by body of wise and expert practitioner.

- ✓ It require certain information to be disclosed in the financial statement

- ✓ It ensures that financial statement reveal true and fair view of affairs of the concern.
- ✓ It ensure financial statement indicate same meaning and same ideas to all the users in domestic and international sphere.so that financial statement of different concerns in different countries can be meaningfully analysed and used for taking decisions.

- ✓ Restrict alternative solution of a particular accounting problem.
- ✓ It make financial statement more rigid and rule oriented
- ✓ AS obfuscate the judgement of the auditors as the standards are mandatory.

- ✓ International Financial Reporting Standards (IFRS) are a set of accounting rules for the financial statements of public companies that are intended to make them consistent, transparent, and easily comparable around the world.

- ✓ IFRS Standards contribute to economic efficiency by helping investors to identify opportunities and risks across the world, thus improving capital allocation. Use of a single, trusted accounting language lowers the cost of capital and reduces international reporting costs for businesses.

- ✓ An accounting theory is a notion that uses speculations, methodologies, and frameworks in the study of financial reporting (as well as how financial reporting principles are applied in the accounting industry).
- ✓ Basically, accounting theories serve as a basis for the understanding of financial reporting and how companies channel their financial statements using the appropriate strategies.
- ✓ An in depth study of accounting theory entails a look into existing accounting practices, how they evolved, and the modifications or additions done to them overtime. These accounting principles serve as framework for accurate financial reporting and statements.

- ✓ Evaluate and explain accounting practices
- ✓ Simplify a complex phenomenon
- ✓ Solve the problem created by the happening of various events
- ✓ Pre calculate the effects of an event on future
- ✓ Forecast any future events
- ✓ Helps in investigation,observation,explanation and conclusion of an event.

- ✓ Practice originated
- ✓ Logic to accounting practice
- ✓ flexibility

Procedure for Issuing Accounting Standards

- ✓ ASB shall determine the broad areas in which Accounting Standards need to be formulated and ‘priority in regard to the selection thereof.

- ✓ In the preparation of Accounting Standards, ASB will be assisted by Study Groups constituted to consider specific subjects. In the formation of Study Groups, provision will be made for wide participation by the members of the institute and others.

- ✓ **The draft of the proposed standard will include the following basic points:**
- ✓ A Statement of concepts and fundamental accounting principles relating to the Standard.
- ✓ Definitions of the terms used in the Standard.
- ✓ The manner in which the accounting principles have been applied for.
- ✓ The presentation and disclosure requirements in complying with the Standard.
- ✓ Class of enterprises to which the Standard will apply.
- ✓ Date from which the Standard will be effective.
- ✓ After taking into consideration the comments received, the draft of the proposed Standard will be finalized by ASB and submitted to the Council of the Institute.
- ✓ The Council of the Institute will consider the final draft of the proposed Standard, and it found necessary, modify the same in consultation with ASB. The Accounting Standard on the relevant subject will then be issued under the authority of the Council.

IFRS and Convergence with AS

Convergence With IFRS

Benefits of Convergence

1] Beneficial to the Economy

If the accounting standards are converged it will promote international business and increase the influx of capital into the country. This will help India's economy grow and expand. International investing will also mean more capital for domestic companies as well.

2] Beneficial to Investors

Convergence is a boon for investors who wish to invest in foreign markets or economies. It makes it much easier for them to study and compare the financial statements of foreign companies. Since the financial statements are made using the same set of standards it is also easier for the investors to understand and analyze them.

3] Beneficial to the Industry

With globally accepted standards the industry can also surge ahead. So convergence is important for the industry as well. It will allow the industry to lower the cost of foreign capital. If companies are not burned by adopting two different sets of standards it will allow them easier entry into the market.

4] More Transparency

Convergence will benefit the users of the financial statements as well. It will make it easier for them to understand the financial statements. And this will generate better transparency and raise the confidence of the investors to invest funds.

5] Cost Saving

Firstly it will exempt companies from maintaining separate accounting books according to separate standards. This will save a lot of work hours and money for the finance department. And also planning and executing auditing will also become easier.

It will be especially helpful for those companies that have subsidiaries in many countries. And the cost of capital will also reduce since capital would be more accessible and easily available.

BASIS FOR COMPARISON	GAAP	IFRS
Acronym	Generally Accepted Accounting Principles	International Financial Reporting Standard
Meaning	A set of accounting guidelines and procedures, used by the companies to prepare their financial statements is known as GAAP.	IFRS is the universal business language followed by the companies while reporting financial statements.
Developed by	Financial Accounting Standard Board (FASB).	International Accounting Standard Board (IASB).
Based on	Rules	Principles
Inventory valuation	FIFO, LIFO and Weighted Average Method.	FIFO and Weighted Average Method.
Extraordinary items	Shown below.	Not segregated in the income statement.
Development cost	Treated as an expense	Capitalized, only if certain conditions are satisfied.
Reversal of Inventory	Prohibited	Permissible, if specified conditions are met.

Accounting Equation

An Accounting Equation is also called the Balance Sheet Equation. We all know that we record all the business transactions using the Dual Aspect concept. This means that each debit has an equal credit and vice-versa.

There are two approaches to record the transactions in financial accounting. One is the Traditional approach or the British Approach and another is the Modern Approach or the American Approach. Under the Modern Approach, we do not debit and credit the accounts. Here, we use the Accounting Equation to debit or credit an account. Thus, it is also called the Accounting Equation Approach.

This approach classifies the accounts as follows:

Assets Accounts: Assets are the properties, possessions or economic resources of a business which help in business operations and in earning revenues. These are measurable in terms of money. However, assets of a firm may be tangible or intangible. Also, we can classify the assets as Fixed Assets and Current Assets. For example, land, building, furniture and fixtures, plant and machinery, vehicles, debtors, bills receivable, bank balance, cash, stock, etc.

Liabilities Accounts: Liabilities are the amounts that an entity owes to the outsiders or the obligations or the debts payable by the entity. We can also classify the liabilities as Long-term and Current. For example, debentures, bank loans, creditors, bills payable, rent outstanding, short-term loans, bank overdraft, etc.

Capital Accounts: Capital or Owner's Equity is the money that the owner brings into the business. The owner can bring Capital in the form of cash or assets. It is an obligation of the business and the business has to pay back this amount to the owner as business is a separate entity from its owner. Therefore, we show the Capital on the liabilities side of the Balance Sheet. Also, we show Capital account after deducting the Drawings by the owner. Drawings are the amount of cash, goods or assets that the owner takes for personal use from the business. Also, the profits increase the Capital and losses decrease it.

The Accounting Equation is:

Assets = Liabilities + Capital (Owner's Equity)

Or

Capital = Assets – Liabilities

Example on Accounting Equation:-

- ✓ **Commenced business with cash ₹500000**
- ✓ **Purchased goods ₹25000**
- ✓ **Paid salary ₹10000**
- ✓ **Sold goods costing ₹20000 at a profit of 25% on the cost**
- ✓ **Paid salary in advance ₹2000**
- ✓ **Introduced additional capital ₹10000**
- ✓ **Purchased computer ₹15000**
- ✓ **Deposited ₹50000 into the bank**

- ✓ It increases the Cash thus, add to cash. Also, it increases the Capital, hence add to Capital.
- ✓ Goods are purchased thus, cash is decreasing. While, goods are coming in thus, they are increasing. Therefore, deduct cash and add goods.
- ✓ Salary is paid therefore cash is decreasing. While salary is an expense. Thus, deduct cash and also deduct from Capital.
- ✓ Goods are going out thus, deduct them. Thus cash is coming in, add it. Also, add the profit to Capital.
- ✓ Salary is paid in advance which is a current asset. Deduct Cash is and add salary paid in advance.
- ✓ Cash and Capital both are increasing. Hence, add Cash and Capital.
- ✓ Cash is decreasing while the computer is increasing. Therefore, deduct cash and add to the computer.
- ✓ Cash is decreasing and bank balance is increasing. Therefore, deduct cash and add to the bank.

ASSETS							LIABILITIES + CAPITAL	
	Cash	Stock	Computer	Pre-paid Salary	Bank	Total	Capital	Total
1.	500000					500000	500000	500000
2.	(25000) 475000	25000 25000				500000	500000	500000
3.	(10000) 465000	25000				490000	(10000) 490000	490000
4.	25000 490000	(20000) 5000				495000	5000 495000	495000
5.	(2000) 488000	5000		2000 2000		495000	495000	495000
6.	10000 498000	5000		2000		505000	505000	505000
7.	(15000) 483000	5000	15000	2000		505000	505000	505000
8.	(50000) 433000	5000	15000	2000	50000	505000	505000	505000

Classification of Accounting

- ✓ **Natural Personal Accounts:** Natural Persons are human beings. Therefore, we include the accounts belonging to them under this head. For instance, Debtors, Creditors, Capital A/c, Drawings A/c, etc.
- ✓ **Artificial Personal Accounts:** Artificial persons are not human beings but can act and work like humans. They have a separate identity in the eyes of law and are capable to enter into agreements. These include H.U.F, partnership firms, insurance companies, co-operative societies, companies, municipal corporations, hospitals, banks, government bodies, etc. For example, Bank of Baroda, Oriental Insurance Co,
- ✓ **Representative Personal Accounts:** These accounts represent the accounts of natural or artificial persons. When the expenses become outstanding or pre-paid and incomes become accrued or unearned, they fall under this category. For example, Outstanding Salary A/c, Pre-paid Rent A/c, Accrued Interest A/c, Unearned Brokerage A/c, etc.

- ✓ **Real Accounts:** These are the accounts of all the assets and liabilities of the organization. We do not close these accounts at the end of the accounting year and appear in the Balance Sheet. Thus, we carry forward the balances of these accounts to the next accounting year. Therefore, we can also say that these are permanent accounts. We can further classify these into:
- ✓ **Tangible Real Account:** It consists of assets, properties or possessions that can be touched, seen and measured. For example, Plant A/c, Furniture and Fixtures A/c, Cash A/c, etc.
- ✓ **Intangible Real Account:** It consists of assets or possessions that cannot be touched, seen and measured but possess a monetary value and thus can be purchased and sold also. For example, Goodwill, Patents, Copyrights, etc.
- ✓ **Nominal Accounts:** Nominal Accounts are the accounts relating to the expenses, losses, incomes, and gains. These are temporary accounts and thus we need to transfer their balances to Trading and Profit and Loss A/c at the end of the accounting year. Therefore, these accounts have no balance to be carried forward next year as they are closed.

Accounts	Debit	Credit
Personal	Receiver	Giver:
Real	What comes in	What goes out
Nominal	Expenses and Losses	Incomes and Gains

Rules for Debit and Credit for all types of accounts:-

Personal Account:

Debit the Receiver

Credit the Giver

Real Account:

Debit what comes in

Credit what goes out

Nominal Account:

Debit all expenses and losses

Credit all incomes and gains

- ✓ Mr D commenced business with cash ₹ 1, 00,000.
- ✓ Purchased machinery for cash ₹ 10,000
- ✓ Purchased goods from Mr A on credit ₹ 50,000
- ✓ Sold goods for cash ₹ 10000
- ✓ Paid wages to Jaimin ₹ 15,000
- ✓ Paid to Mr A ₹ 25000
- ✓ Wages to be paid to Mr C is outstanding ₹ 5000
- ✓ Brokerage earned but not received ₹ 2000
- ✓ Deposited ₹ 15000 into the bank.
- ✓ Mr D withdrew cash for personal use ₹ 10000

Analysis of transactions

Transaction	Accounts	Nature of Accounts	Reason for Effect on Accounts	Debited or Credited
1.	Cash A/c Capital A/c	Real A/c Personal A/c	Cash is coming in Mr D is the giver	Debit Credit
2.	Machinery A/c Cash A/c	Real A/c Real A/c	Machinery is coming in Cash is going out	Debit Credit
3.	Purchases A/c Mr A's A/c	Real A/c Personal A/c	Goods are coming in Mr A is the giver	Debit Credit
4.	Cash A/c Sales A/c	Real A/c Real A/c	Cash is coming in Goods are going out	Debit Credit
5.	Wages A/c Cash A/c	Nominal A/c Real A/c	Wages are an expense Cash is going out	Debit Credit
6.	Mr A's A/c Cash A/c	Personal A/c Real A/c	Mr A is the receiver Cash is going out	Debit Credit
7.	Wages A/c Wages Outstanding A/c	Nominal A/c Representative Personal A/c	Wages is an expense Wages is payable to Mr C and thus he is our creditor.	Debit Credit
8.	Accrued Brokerage A/c Brokerage A/c	Representative Personal A/c Nominal A/c	Brokerage is receivable from the client, so the client is our debtor Brokerage is an income	Debit Credit
9.	Bank A/c Cash A/c	Personal A/c Real A/c	The bank is receiving the amount Cash is going out	Debit Credit
10.	Drawings A/c Cash A/c	Personal A/c Real A/c	Mr D is the receiver Cash is going out	Debit Credit

Debit and Credit

- A debit is an accounting entry that either increases an asset or expense account. Or decreases a liability or equity account. It is positioned on the left in an accounting entry.
- A credit is an accounting entry that increases either a liability or equity account. Or decreases an asset or expense account. It is positioned on the right in an accounting entry.

The following are the rules of debit and credit which guide the system of accounts, they are known as the Golden Rules of accountancy:

- First: Debit what comes in, Credit what goes out.
- Second: Debit all expenses and losses, Credit all incomes and gains.
- Third: Debit the receiver, Credit the giver.

A debit and credit entry have a broad impact on different accounts. For example, in

- Asset accounts, a debit increases the balance and a credit decreases the balance.
- Liability accounts, a debit decreases the balance and a credit increases the balance.
- Equity accounts, a debit decreases the balance and a credit increases the balance.
- Revenue accounts, a debit decreases the balance and a credit increases the balance

a. Cash Sale

b. Cash Purchase

c. Repayment of loan

Solution:

Sale for cash

Cash A/c – Dr.

To Sale A/c

2. Purchase of inventory from the supplier for cash

Inventory A/c – Dr.

To Cash A/c

3. Repaying a loan

Loan payable A/c – Dr.

To cash A/c

Double Entry System

Double Entry System of accounting deals with either two or more accounts for every business transaction.

ASSETS = LIABILITIES + EQUITY

A systematic accounting process, the activities are recorded into various accounts to keep the data bifurcated and classified under account heads. There are majorly seven types of accounts wherein all the business accounting entries and transactions are classified. These are:

- Assets
- Liabilities
- Equity
- Gains
- Losses
- Expenses
- Revenues

Debit and Credit

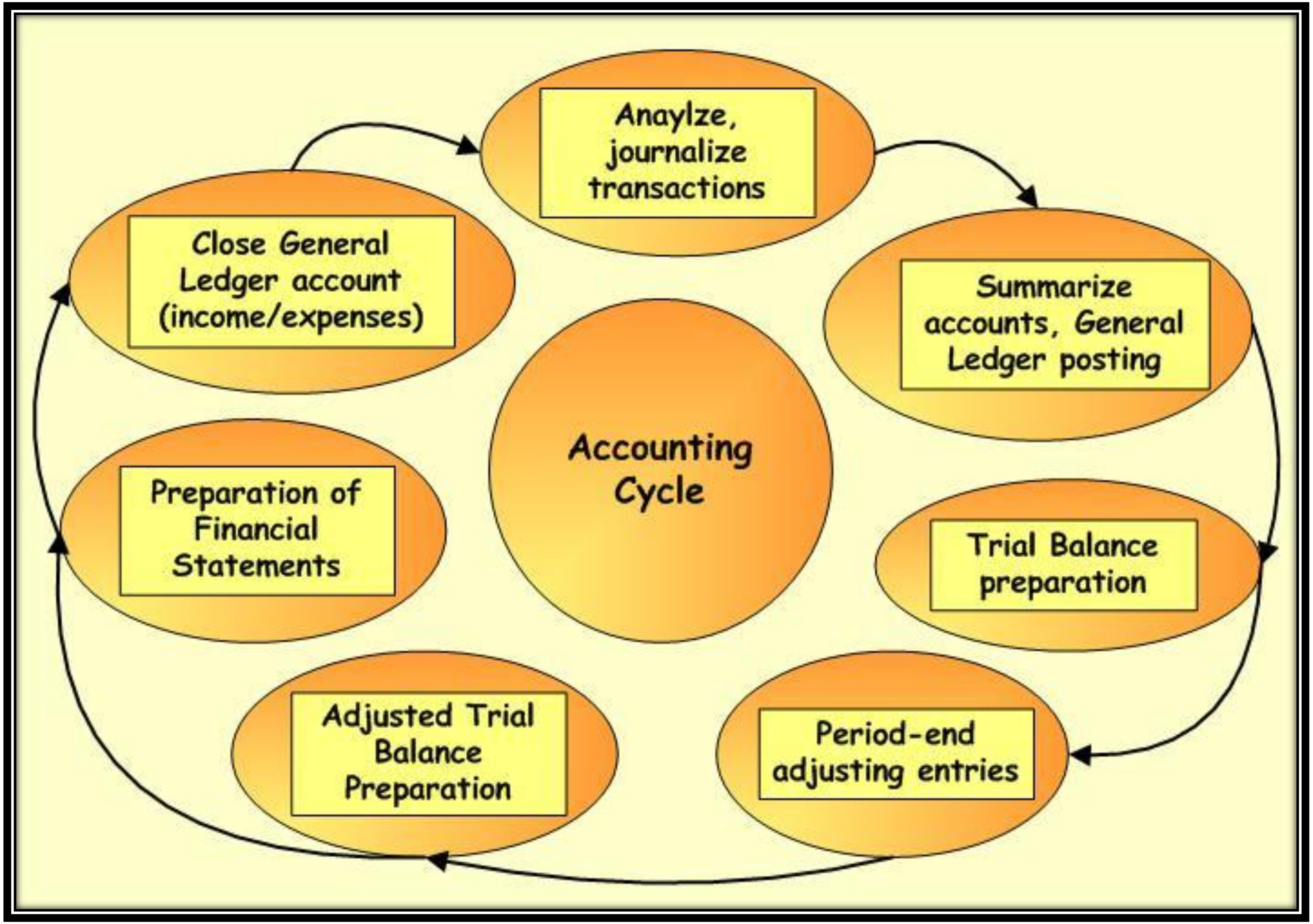
Debits and Credits are essentials to enter data in a double entry system of accounting and book-keeping. While posting an accounting entry, an entry on the left side of the account ledger is a debit entry and right side entry is a credit entry.

Advantages of Double Entry System

- This system increases the Accuracy of the accounting, through the trial balance device
- Profit and loss suffered during the Year can be calculated with details
- By following this system the company can keep the accounting records in detail which eventually helps in controlling

Accounting Cycle

Accounting cycle is a process of recording all the financial transactions and processing them. When a complete sequence of recording and processing financial transactions is followed which happens frequently on a continuous basis during an accounting period is known as the accounting cycle. It thus begins with the occurrence of financial transactions, from when it occurs, its representation on the financial statements and closing the accounts of an entity.


Anaylze, journalize transactions
Summarize accounts, General Ledger posting
Trial Balance preparation
Period-end adjusting entries
Adjusted Trial Balance Preparation
Preparation of Financial Statements
Close General Ledger account (income/expenses)
Accounting Cycle

Recording of transactions

Journal

Next step in this accounting cycle is to record the financial transactions in the journal. We record financial transactions in Journal chronologically.

There can be one or more than one accounts debited and one or more accounts can be credited. An accountant shall check that both the debit and the credit balance match.

Ledger

All the journal entries prepared in the earlier step are posted into respected ledgers chronologically. A ledger shows the summary of all the financial transactions related to such account. For example: – In cash ledger, we find a summary of all the cash transactions.

Trial balance

After completion of the posting of entries to ledgers, we need to prepare a trial balance. We prepare trial balance after considering all the ledger account closing balances.

We prepare it at the end of the accounting period for the preparation of financial statements. Accounting period may be monthly, quarterly or yearly based on the entity's requirements.

Adjustment Entries

We need to record the adjustment entries properly. We need to make these entries before the preparation of financial statements of an entity. At the end of the accounting period, adjusting entries must be posted to the ledgers.

Adjusted Trial Balance

After preparation of trial balance and making adjustment entries (if any), an adjusted trial balance may also be prepared. An accountant shall also check that the debit and credits on the trial balance match.

Closing Entries

We shall make proper entries for the closure of nominal accounts. We shall close accounts by transferring the balances to Trading Account & Profit and Loss Account.

Financial Statements

After following the above steps, we can prepare financial statements easily. Financial statements will show the true financial position and operating results of the entity's business.

Journal

Journal is the book of primary entry in which we record all transactions before posting them into the ledger. We need to keep a journal in a columnar form. There are some function and advantages of journal day book

Functions of Journal

(i) Analytical Function: While recording a transaction in the journal each transaction is analyzed into the debit aspect and the credit aspect. This helps to find out how each transaction will financially affect the enterprise.

(ii) Recording Function: Accountancy is a business language which helps to keeps the record of the transactions based on the principles. Each such recording entry is supported by a brief narration, which explains, every transaction in simple language.

(iii) Historical Function: Journal book contains a chronological record of the transactions for future references.

Advantages of the Journal

The following are the advantages of a journal:

(i) Chronological Record: Journal book records transactions as and when it happens. Therefore it is possible to get day-to-day information.

(ii) Minimizing the possibility of errors: The nature of the transaction and its effect on the financial position of the business is ascertained by recording and analyzing into debit and credit aspect.

(iii) Narration: It means the explanation of every recorded transaction.

(iv) Helps to finalize the accounts: It is the basis of ledger posting and the ultimate Trial Balance.

- Journal records all business transactions in one place on the time and date basis.
- All transactions which are recorded, are supported with a receipt or bill, so we can check the authenticity of each journal entries with their bills.
- There is a minimum chance to avoid any particular transaction because in a journal we record every transaction on a date basis.
- Accountant writes each journal entry’s narration below that journal entry, so another auditor can know what is the reason of that journal entry.
- In a journal, we record each transaction after deep analysis of two accounts on the basis of double entry system, so there is a minimum chance of mistake in the journal.
- Journal is the basis of posting transactions in ledger accounts. Without making of the journal, an accountant can not make ledger accounts.
- If there is a mistake in ledger accounts, we can easily rectify it with the help of journal or rectify journal entry in the journal.
- All opening journal entries, closing journal entries and all other transactions which we cannot record in any other subsidiary books, we record them in the journal proper.

Date	Particulars	L.	Dr.	Cr.
		F.	Amount	Amount
			Rs	Rs

Jan. 1 Commenced business with a capital 20,000

3 Amount deposited in S.B.I 5,000

6 Goods purchased for cash 7,000

10 Furniture purchased from Chinmoy 5,000

11 Goods sold to Anil Majumdar for cash 8,000

13 Goods sold to Ashim Das 2,000

25 Cash drew for private uses 500

31 Salaries paid 800

Journal

Date	Particulars		L. F.	Dr. Amount ₹	Cr. Amount ₹
1997 Jan. 1	Cash Account	Dr.		20,000	
	To Capital Account				20,000
	(Being capital invested)				
3	Bank Account	Dr.		5,000	
	To Cash Account				5,000
	(Being cash deposited into bank)				
6	Purchase Account	Dr.		7,000	
	To Cash Account				7,000
	(Being goods purchased for cash.)				
10	Furniture Account	Dr.		5,000	
	To Chinmoy's Account				5,000
	(Being furniture purchased from Chinmoy.)				
11	Cash Account	Dr.		8,000	
	To Sales Account				8,000
	(Being goods sold to Mazumdar on cash.)				
13	Ashim Das' Account	Dr.		2,000	
	To Sales Account				2,000
	(Being goods sold to Ashim Das.)				
25	Drawings Account	Dr.		500	
	To Cash Account				500
	(Being cash drew for personal use)				
31	Salaries Account	Dr.		800	
	To Cash Account				800
	(Being salaries paid.)				

Ledger Accounts Meaning and Definition

Ledger is a book that contains the accounts. Any financial statement related to the financial position of the company emerges only from the accounts. Thus, this ledger is known as the principal book. So, the result of all this is that it is necessary to relate all the information for any account available is from the ledger. This book of accounts is the most important book for any business and that is why it is known as the king of all books. Also, the ledger book is also known as the book of the final entry.

There are 3 types of Ledgers –

- Sales Ledger
- Purchase Ledger
- General Ledger

1. Sales Ledger – Sales Ledger is a ledger in which the company maintains the transaction of selling the products, services or cost of goods sold to customers. This ledger gives the idea of sales revenue and income statement.

2. Purchase Ledger – Purchase Ledger is a ledger in which the company organizes the transaction of purchasing the services, products, or goods from other businesses. It gives the visibility of how much amount the company paid to other businesses.

3. General Ledger – General Ledger is divided into two types – Nominal Ledger and Private Ledger. Nominal ledger gives information on expenses, income, depreciation, insurance, etc. And Private ledger gives private information like salaries, wages, capitals, etc. Private ledger is not accessible to everyone.

Ledger Account Examples

Assets

- Cash
- Land
- Accounts receivable
- Equipment

Liabilities

- Debt
- Accounts Payable
- Loans
- Accrued expenses

Stock

- Stockholders Equity
- Common Stocks
- Retained Earnings

Operative Revenues

- Sales
- Services Fees

Operating Expenses

- Salaries and wages
- Office Expenses
- Depreciation Expense

Liabilities: This decreases on the side of debt and increases on the credit side.

Assets: In assets, the figure increases on the left side or you can say the debit side. While this decreases on the credit size or the right side.

Capitals: This follows the same rule as liabilities.

Gains or Income: In this, there is a decrease on the debit side. Also, there is an increase in the credit side.

Expenses: The expenses in the ledger decreases on the credit side while increases on the debit side.

There are some rules that students should understand according to the nature of debit and credit.

Debits and Credits

Credit

- For properties and goods, the credit represents that the value and stock of goods and properties have decreased. This is moreover related to real accounts.
- In the case of different accounts like dividend or interest or commission received, or the discount to be gained, it is reported that the firm has made again. This is moreover related to the nominal account.

Debit

- For goods or properties, the value and use of such goods have been increased. This is related to real accounts.
- Also, there is a case in which a person has received some benefit against some service given by him or will be rendered by him in the future. Thus, when a person is liable to do something for a firm, the fact is mentioned using that person’s account. This is moreover related to the personal account.
- For other accounts like expenses or losses, a certain expense has been incurred by the firm or has lost money. This can be related to the nominal account.

Ledger

Dr. **Cr.**

Date	Particulars	LF	Amount	Date	Particulars	LF	Amount
			₹				₹

Sales Day Book

Sales day book is also known as a sales book, sales journal, sold book etc. It is a subsidiary book, i.e. a book of original entry. It is a manually maintained account, with the purpose of recording all credit sales of the business in one place.

This means all the sales of the firm done on credit are recorded in the sales day book. No cash sales will be recorded here, they are recorded in the cash book. And only the sale of goods will be recorded here.

- Sold goods to X for 600/-
- A credit sale of 10 units to Y for 35/- per unit
- Sold 50 units to Z for 1350/- inclusive of 10% cash discount
- Q bought units worth 500/- on credit

Date	Buyer Names	Invoice	LF	Amount
01/01	X			600/-
02/01	Y (10×35)			350/-
03/01	Q			500/-
	Total			1450/-

Sales Day Book

Note that the goods sold to Z will not be a part of the sales book as the transaction is a cash transaction. So that transaction will be recorded in the cash book.

X’s Account

Date	Particulars	Amount	Date	Particulars	Amount
01/01	To Sales Acc	600			

Y's Account

Date	Particulars	Amount	Date	Particulars	Amount
01/01	To Sales Acc	350			

Q's Account

Date	Particulars	Amount	Date	Particulars	Amount
01/01	To Sales Acc	500			

Purchase Day Book

Purchase day book is also known as purchase journal, purchase book, invoice book, bought book etc. is a type of subsidiary book. It is also a book of original entry.

The purpose of the purchase day book is to record all the credit purchases of the business that are meant for resale.

This means that it does not record any cash purchase transactions. Such transactions will be recorded in the cash book.

Advantages of Purchase Day Book

- All entries of purchases of goods on credit are recorded in one place. It is easy to reference and browse these entries.
- Important information about these transactions (like the number of goods or the rate of purchase etc.) are written in the journal

- Bought 20 computers from ABC Co. at 20,000/- per computer and a 10% trade discount
- Bought 100 phones from LMN Co. at 1000/- on credit
- 350 televisions from DEF Co. at 24500/- each and a 5% cash discount
- Purchased 200 radios from JKL Co. at 500/- each on credit

Date	Name of Supplier	Invoice	LF	Amount
4/6/18	ABC Co. 20,000 × 20 @ 10% discount			3,60,000/-
8/6/18	LMN Co. 100 × 1000			1,00,000/-
15/6/18	JKL Co. 200 × 500			1,00,000
	Total			5,60,000/-

Sales Book

- ✓ A Sales Book is a Subsidiary Book and is, therefore, also a book of Original Entry. A Sales Book or Sales Day Book contains the records of all-credit sales of goods. While a Cash Book holds the records of all-cash sales of goods.

- ✓ The entries in the Sales Book are also made with the net amount of the invoice. Therefore, Sales Book does not contain a Trade Discount and other details are given on the invoice.

Sales Book

Date	Invoice No.	Name of the Customer	L.F.	Amount

Sales Return Book

A Credit Note is prepared for every return of goods. It is prepared in duplicate. The Credit Note contains the name of the customer, details of goods returned and reason thereof. Each Credit Note is dated and serially numbered. The Credit Note serves as the source document for entries in the Sales Return Book.

Sales Return Book

Date	Credit Note No.	Name of the Customer	L.F.	Amount

Date	Details
10 Aug	Sold to A Ltd. (Invoice No. 24): 2000 shirts @ ₹ 500 per piece.
16 Aug	Sold to B Ltd. (Invoice No. 26): 100 ties @ ₹ 200 per piece. Trade discount 20%
18 Aug	Sold to C Ltd. (Invoice No. 28): 50 coats for ₹100000. Trade discount 10%
21 Aug	Sold to D Ltd. (Invoice No. 30): 100 trousers @ ₹ 400 per piece. Trade discount 15%
25 Aug	Sold to E Ltd. (Invoice No. 33): 50 ties @ ₹ 250 per piece. Trade discount 10%

Sales book

Date	Invoice No.	Name of the Customer	L.F.	Amount
10 Aug	24	A Ltd.		1000000
		2000 shirts @ ₹ 500 per piece		
16 Aug	26	B Ltd.		16000
		100 ties @ ₹ 200 per piece. = 20,000		
		Less: 20% T.D. = 4,000		
18 Aug	28	C Ltd.		90000
		50 coats @ ₹ 2,000 per piece = 100000		
		Less: 10% T.D. = 10000		
21 Aug	30	D Ltd.		32000
		100 trousers @ ₹ 400 per piece = 40,000		
		Less: 15% T.D. = 6,000		
25 Aug	33	E Ltd.		11250
		50 ties @ ₹ 250 per piece = 12,500		
		Less: 10% T.D. = 1,250		
31 Aug		Total		1149250

A Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
10 Aug	To Sales	1000000				

B Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
16 Aug	To Sales	16000				

C Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
18 Aug	To Sales	90000				

D Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
21 Aug	To Sales	32000				

E Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
25 Aug	To Sales	11250				

Sales A/c

Date	Particulars	Amount		Date	Particulars	Amount
				31 Aug	Sundries as per Sales Book	1149250

Record the following transactions in the books of M/s. Z and Co. and also show the ledger accounts.

Date	Details
5 Aug	Goods returned by M Ltd. (Credit Note No. 2): 2 bags @ ₹ 500 per piece.
11 Aug	Goods returned by D Ltd. (Credit Note No. 3): 10 suitcases @ ₹ 2500 per piece. Trade discount 20%
28 Aug	Goods returned by X Ltd. (Credit Note No. 5): 5 duffle bags for ₹5000. Trade discount 10%

Sales Return Book

Date	Credit Note No.	Name of the Customer	L.F.	Amount
5 Aug	2	M Ltd.		1000
		2 bags @ ₹ 500 per piece.		
11 Aug	3	D Ltd.		20000
		10 suitcases @₹ 2500 per piece = 25000		
		Less: 20% T.D. = 5000		
28 Aug	5	X Ltd.		4500
		5 duffle bags @ ₹1000 per piece = 5000		
		Less: 10% T.D. = 500		
31 Aug		Total		25500

MNC Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
				5 Aug	By Sales Return	1000

D Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
				11 Aug	By Sales Return	20000

X Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
				28 Aug	By Sales Return	4500

Sales Return A/c

Date	Particulars	Amount		Date	Particulars	Amount
31 Aug	Sundries as per Sales Return Book	25500				

Purchase Book

Purchase book is a Subsidiary book. The Purchase book or Purchase day book contains the record of all credit-purchase. Cash book accommodates the records of all goods-purchase.

A Purchase book does not hold the record of purchases of assets. The Journal proper contains those records. The entries are recorded in the Purchase book from source documents. Invoices or bills received from the suppliers of goods serve as the source documents.

Purchase Book

Date	Invoice No.	Name of the Supplier	L.F.	Amount (₹)

Purchase Return Book

When the goods purchased on credit are returned to the supplier, these are recorded in the Purchase return book. Sometimes, goods purchased can be defective or of low quality, etc. and hence, need to be returned. A separate book is maintained for the purchase return and these are not deducted from the purchases in the Purchase book. Also, Purchase return is recorded at the net amount on the invoice.

Date	Details
1 Aug	Purchased from ABC Ltd. (Invoice No. 524): 2000 balls @ ₹ 5 per piece.
15 Aug	Purchased from XYZ Ltd. (Invoice No. 611): 100 bats @ ₹ 250 per piece. Trade discount 20%
29 Aug	Purchased from Con Ltd. (Invoice No. 444): 200 skates for ₹100000. Trade discount 10%
29 Aug	Purchased from ABC Ltd. (Invoice No. 741): 200 Chess for ₹2000. Trade discount 15%
30 Aug	Purchased from Con Ltd. (Invoice No. 521): 100 skates for ₹40000. Trade discount 8%

Date	Invoice No.	Name of the Supplier	L.F.	Amount (₹)
1 Aug	524	ABC Ltd.		10000
		2000 balls@ ₹ 5 per piece.		
15 Aug	611	XYZ Ltd.		20000
		100 bats@ ₹ 250 per piece. = 25000		
		Less: 20% T.D. = 5000		
29 Aug	444	Con Ltd.		90000
		200 skates @ ₹ 500 per piece = 100000		
		Less: 10% T.D. = 10000		
29 Aug	741	ABC Ltd.		1700
		200 Chess @ ₹ 100 per piece = 2000		
		Less: 15% T.D. = 300		
30 Aug	521	Con Ltd.		36800
		100 skates @ ₹ 400 per piece = 40000		
		Less: 8% T.D. = 3200		
31 Aug		Total		167500

ABC Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
				1 Aug	Purchases	10000
				1 Aug	Purchases	1700

XYZ Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
				15 Aug	Purchases	20000

Con Ltd. A/c

Date	**Particulars**	**Amount**		**Date**	**Particulars**	**Amount**
				29 Aug	Purchases	90000
				30 Aug	Purchases	36800

Purchases A/c

Date	**Particulars**	**Amount**		**Date**	**Particulars**	**Amount**
31 Aug	Sundries as per Purchase Book	167500				

Record the following transactions in the books of M/s. Zen and Co. and also show the ledger accounts:-

Date 2018	**Details**
3 Aug	Returned goods purchased from MNC Ltd. (Debit Note No. 24): 2 T.V. @ ₹ 50000 per piece.
17 Aug	Goods returned purchased from D Ltd. (Debit Note No. 26): 10 DVD Players @ ₹ 2500 per piece. Trade discount 20%
30 Aug	Returned goods purchased from X Ltd. (Debit Note No. 28): 5 refrigerators for ₹60000. Trade discount 10%

In the Books of M/s. Zen and Co.

Purchase Return Book

Date	Debit Note No.	Name of the Supplier	L.F.	Amount (₹)
3 Aug	24	MNC Ltd.		100000
		2 T.V. @ ₹ 50000 per piece		
17 Aug	26	D Ltd.		20000
		10 DVD Players @ ₹ 2500 per piece. = 25000		
		Less: 20% T.D. = 5000		
30 Aug	28	X Ltd.		54000
		5 refrigerators @ ₹ 12000 per piece = 60000		
		Less: 10% T.D. = 6000		
		Total		174000

Ledger Accounts
MNC Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
3 Aug	Purchases Return	100000				

D Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
17 Aug	Purchases Return	20000				

X Ltd. A/c

Date	Particulars	Amount		Date	Particulars	Amount
30 Aug	Purchases Return	54000				

Purchases Return A/c

Date	Particulars	Amount		Date	Particulars	Amount
				31 Aug	Sundries as per Purchase Return Book	154000

Journal Proper

A Journal proper in the accounting system is a book of original entry in which all type of miscellaneous credit transactions, which usually do not fit in any other books are recorded.

Opening Entries

These entries include entries for opening a new business. For example, a business is opened with Cash Rs 100, debtors Rs 200, stock Rs 300 bank loan Rs 400 and capital Rs 200

Date	Particulars		Debit	Credit
1st April	Cash A/c	Dr	100	
	Debtors A/c	Dr	200	
	Stock A/c	Dr	300	
	To Loan A/c			400
	To Capital A/c			200

Closing Entries

At the end of the year, certain closing entries will be required to transfer the balance of all the income and expenses accounts to trading and profit and loss account. For example on 31st December the balance in expenses accounts are Salary Rs 500, rent Rs 200, Stationary Rs 50, legal charges Rs 100, and income accounts are commission received Rs 50.

Date	Particulars		Debit	Credit
31st March	Profit & Loss A/c	Dr	850	
	To Salary A/c			500
	To Rent			200
	To Stationary			50
	To Legal Charges A/c			100

Date	Particulars		Debit	Credit
31st March	Commission Received A/c	Dr	50	
	To Profit & Loss A/c			50

- ✓ Transfer Entries

When accounts are transferred from one account to another fora combination of allied items, it is necessary to pass transfer entry. Such Entries are passed in the Journal proper for the sake of record keeping.

- ✓ Adjustment Entries

Modification of the accounts at the end of an accounting period is called adjustments. If there are any events affecting the related period of accounts but left out of the books, the same should be incorporated in the books before the preparation of the final accounts. This is done by means of adjusting entries through the journal proper.

Examples of transfer entries and adjusting entries.

Date	Particulars		Debit	Credit
21st March	Capital A/c	Dr	50,000	
	To DrawingsA/c			50,000

Example of an adjusting entry is rent outstanding.

Date	Particulars		Debit	Credit
31st March	Rent A/c	Dr	8500	
	To Rent Outstanding A/c			8500

Trial Balance

When using the Double Entry System of Accounting at the end of the year, the firm prepares a bookkeeping worksheet of all the debit and credit balances of all the ledgers. This is a trial balance statement, a summary of the closing balances of all accounts. Let us learn more about its features, preparation, and significance.

Objectives of Trial Balance

i. It ensures that the posting from the ledgers is done correctly. If there are any arithmetic errors in the accounting then this will get reflected in the trial balance. And we can determine this when the total of the debit column and the credit column do not match.

ii. Similarly, it will also detect clerical errors, like a fault in posting, mixing up of figures, etc.

iii. Trial balance will also help in the preparation of the final accounts. The balances for the financial statements are taken from the trial balance.

iv. And the trial balance will also serve as a useful summary of all accounting records. It is a summary of all the ledger accounts of a firm. We will only refer to the individual ledger accounts if any details are needed. Otherwise, we rely on the trial balance.

Limitations of Trial Balance

- A transaction that is completely missing, was not even journalized
- When the wrong amount was written in both the accounts
- If a posting was done in the wrong account but in the right amount
- An entry that was never posted in the ledger altogether
- Double posting of entry by mistake

Definition of Cash Accounting

The basis of accounting in which the recognition of revenues and expenses are done only when there is actual receipt or disbursement of cash takes place. In this method, in which the income or expense is recognised when the inflow or outflow of cash exists in reality.

- It does not coincide with matching concept.
- Time lags in the occurrence of a transaction and its recognition.
- Lacks in accuracy.

Definition of Accrual Accounting

Accrual Accounting is the base of present accounting. It is also known as the mercantile system of accounting wherein the transactions are recognised as and when they take place. Under this method, the revenue is recorded when it is earned, and the expenses are reported when they are incurred.

- Unearned Income
- Accrued Income
- Prepaid Expenses
- Outstanding Expenses

BASIS FOR COMPARISON	CASH ACCOUNTING	ACCRUAL ACCOUNTING
Meaning	The accounting method in which the income or expense is recognized only when there is actual inflow or outflow of cash.	The accounting method in which the income or expense is recognized on mercantile basis.
Nature	Simple	Complex
Method	Not recognized method as per companies act.	Recognized method as per companies act.
Income statement	Income statement shows lower income.	Income statement will show a comparatively higher income.
Applicability of matching concept	No	Yes
Recognition of revenue	Cash is received	Revenue is earned
Recognition of expense	Cash is paid	Expense is incurred
Degree of Accuracy	Low	Comparatively high

Example:-

Mr X is a Lawyer. Particulars of the Income And Expenses for the year ended 31/12/2016

1.Fees Received from clients in cash Rs.64800/-

2.Salary of Clerks And Assistant Paid Rs.24000/-

3.Rent of Chamber Paid (Gross) Rs.27000/-

4.Salary And Clerks And Assistants Outstanding Rs.2160/-

5.Accured Fees Rs.14400/-

6.Rent of Chamber Paid in Advance Rs.1800/- (Including Above)

7.Misc Expenses Rs.5040/-

8.Telephone Charges Rs.2880/-

Particulars	Amount (Rs)	Amount (Rs)
Fees Received in Cash	64800	
Add:- Accured Fees	14400	79200
Less:-		
Expences	24000	
Add:- Outstanding	2160	-26160
Rent of Chamber Fees	27000	
Less:- Paid In Advance	1800	-25200
Misc Expences	5040	
Telephone Charges	2880	-7920
Net Income Under Accrual Basis		19920

Particulars	Amount (Rs)	Amount (Rs)
Net Income Under Accural Basis		19920
Add:- Outstanding Salary		2160
		22080
Less:-Rent Paid In Advance	1800	
Accrued Fees Not Yet Received	14400	-16200
Net Income Under Cash Basis		5880