

## FUNDAMENTALS

### ACCOUNTING PROCESS-1

Source documents  
↓  
Transactions & other events

Journal

Ledger

Trial balance

Final a/c

Trading  
& Profit  
& loss a/c

Balance  
Sheet

### ACCOUNTING PROCESS-2

Source documents  
↓  
Transactions & other events

Subsidiary books

Ledger

Trial balance

Final a/c

Trading  
& profit  
& loss a/c

Balance  
sheet.

### SOURCE DOCUMENTS :

\* Source documents are documents (paper or instrument) through which we identify transactions and other events.

Eg: Voucher, debit note, credit note, agreement, purchase bill, sales bill, passbook.

## VOUCHER:

- \* Voucher is a written document in a support of a transaction.
- \* Voucher is an internal evidence.
- \* When external evidence is not provided, we should create internal evidence (voucher).
- \* But, it is advisable to create internal evidence (voucher), even though external evidence is provided to avoid fraudulent for all transactions.

## DEBIT NOTE:

- \* Whenever we debit any party in our books of accounts (journal & ledger), for any reason we send a note to that party stating his account has been debited in our account and that note is called as debit note.

## TRANSACTIONS AND OTHER EVENTS:

- \* Financial events = Transactions + other events
- \* All transactions are events, but not all events are transactions.

## BUSINESS TRANSACTIONS:

- \* Transaction = Trans (Between) + Action (Activities).
- \* Business transactions means business activities.
- \* It involves another person.
- \* Give / take / give and take.
- \* Cash, goods (any item held for sale), properties (assets held for use), services or benefits (for which money value can be assigned)

## MONETARY TRANSACTIONS:

- \* Monetary transactions are transactions for which money value can be assigned.
- \* In accounting, we record only monetary transaction.
- \* Non-monetary transactions are not recorded.
- \* Monetary transactions are classified into two.  
They are: i) Cash transaction  
ii) Credit transaction.

## OTHER EVENTS:

- \* It does not involve other person.
- \* Other events are consequences or results arising out of transactions.
- \* Eg: Goods destroyed by fire, closing stock, profit on sale of assets.

## JOURNAL :

- \* Journal is a French word which means daily.
- \* Journal is a notebook wherein we record transactions & other events of financial nature in chronological order (Date sequence) and in a systematic manner.

## JOURNALISING :

- \* Journalising is a process of recording the transactions & other events in a financial nature in a chronological order & in a systematic manner.

## JOURNAL ENTRY :

- \* Journal entry is an entry made in journal notebook or recorded transactions.

## DOUBLE ENTRY SYSTEM OF BOOK KEEPING :

- \* To enter transactions & other events in a journal, we use double entry system of book keeping.

- \* Luca Fra Pacioli, Italian small trader founded the concept of double entry system of book keeping in 15th century.
- \* He is also known as father of accounting.
- \* The main principle of double entry system of book keeping is for every debit there must be a corresponding credit with equal amount or vice versa.
- \* Double entry system is called as dual aspect concept (idea).
- \* The word debit and credit are derived from Latin word deb'ne (DR.) and crede're (CR.) respectively.
- \* Luca Fra Pacioli told that there is no need for us to assign the meaning for debit & credit.

<u>DEBIT</u>	<u>CREDIT</u>
* Right	* Left
* Incoming aspect	* Outgoing aspect.
* Receiving aspects	* Giving aspect.
* Expenses	* Incomes.

These are the wrong meanings for debit & credit

## ACCOUNT:

- \* Account is a ledger account.
- \* Transactions of similar nature are grouped & taken to the particular place in ledger is called account.
- \* Account is summary of transactions relating to a particular item grouped at a particular place.
- \* Accounts are classified into 3. They are :
  - i> Personal account.
  - ii> Real account.
  - iii> Nominal account.

## PERSONAL ACCOUNT:

### i> NATURAL PERSONAL ACCOUNT:

\* These accounts relate to natural persons (Human being).

\* Eg: Mohan's a/c, Sekar's a/c ...

### ii> ARTIFICIAL PERSONAL ACCOUNT:

\* These accounts are organisations formed by persons.

\* Eg: Bank a/c, K.S. Club's a/c ...

### iii) REPRESENTATIVE PERSONAL ACCOUNT:

\* Representative personal account should be either asset or liability and behind that there must be a person.

\* Eg: Bank loan, drawings, capital, bills receivable, bills payable, outstanding and prepaid incomes and expenses, PBDP ...

### REAL ACCOUNT:

\* Real account includes assets.

\* They are further classified into two. They are:

i) Tangible real account.

ii) Intangible real account.

\* Eg: Cash at c, good, properties, biological assets like living plants & animals ...

### NOMINAL ACCOUNT:

\* Nominal account includes expenses, incomes, losses and gains.

\* Eg: Salary, interest paid, insurance account, telephone expenses account, commission paid or received account, travelling charges account

## PROPERTIES:

\* Properties are assets held for use which have more than one year life time according to materiality concept.

## EXPENSES:

\* Amount spent for which we enjoy a benefit for a short period of time either a year or less than a year is called expenses.

## LOSSES:

\* Amount spent for which we enjoy no benefit is called losses.

## INCOME:

\* Amount earned by providing <sup>di</sup> benefit is called income.

## GAIN:

\* Amount earned by without providing any benefit is called gains.

[Just for understanding.

Not for examination purpose]



## GOLDEN RULES FOR DOUBLE ENTRY SYSTEM:

### i) PERSONAL ACCOUNT:

- \* Debit the receiver
- \* Credit the giver.

### ii) REAL ACCOUNT:

- \* Debit what comes in.
- \* Credit what goes out.

### iii) NOMINAL ACCOUNT:

- \* Debit all expenses & losses.
- \* Credit all incomes & gains.

## CREDITOR:

- \* If we have to pay money to any person, that person is our creditor.
- \* Creditor is someone who lends money.

## DEBTOR:

- \* If any person have to pay money to us, that person is our debtor.
- \* Debtor is someone who owes money.

[In journal entry, for cash transaction, cash must be one aspect]

## BUSINESS ENTITY CONCEPT:

- \* The business entity concept states that the business is separate from the owner of the business.
- \* Therefore, the transactions associated with a business must be separately recorded from those of its owners or other businesses.

## LEDGER:

- \* The process of transferring journal entries into ledger account is called posting.
- \* The ledger account is of 'T' format.
- \* Journal is a instructions.
- \* Execution of that instructions is called posting.
- \* When we post debit aspect of journal entry, there is no need for us to see credit aspect of journal entry.
- \* Debit & credit posting is independent of each other.

## TRIAL BALANCE:

- \* A trial balance is a list of all the general ledger accounts contained in the ledger of a business.

\* Trial balance is a statement prepared periodically, usually at the end of every reporting period.

#### SUBSIDIARY BOOKS:

- \* Subsidiary books are special & small journal.
- \* Division of labour, labour check and time saving are the advantages of subsidiary books.

#### i) PURCHASE DAY BOOK:

\* In purchase day book, only credit purchase of goods & services should be recorded.

#### ii) SALES DAY BOOK:

\* In sales day book, only credit sale of goods & services should be recorded.

#### iii) PURCHASE RETURN DAY BOOK:

\* In purchase return day book, only credit purchase return of goods should be recorded.

\* In transaction, if it is not mentioned, whether it is credit or cash purchase return, we should assume it as credit.

#### iv) SALES RETURN DAY BOOK:

- \* In sales returns day book, only credit sales returns of goods should be recorded.
- \* In transaction, if it is not mentioned, whether it is credit or cash sales, we should assume it as credit sales.

#### v) CASH BOOK:

- \* Cash book is a cash account.
- \* Cash book is a journal cum ledger. So, particulars is important.
- \* In cash book, we record all receipts (cash) in left side and all payments (cash) in right side.
- \* In cash book, payments cannot be more than receipts. Hence, credit balance is impossible in the cash column of the cash book.

#### SINGLE COLUMN CASH BOOK:

- \* The single column cash book is also called as simple cash book.
- \* It has only one money column on both debit & credit side.

## DOUBLE COLUMN CASH BOOK:

\* If along with amount columns to record cash receipts and payments another column is added on each side to record the cash discount allowed or the discount received, or a column on the debit side showing bank receipts and another column on the credit side showing payments through bank, it is a double-column cash book.

\* Discount allowed and discount received column of the cash book should only be totalled and cash and bank column of the cash book should be totalled and balanced.

\* Because, discount columns are journal and cash & bank columns are journal cum ledger.

## BUSINESS DISCOUNT:

### i) TRADE DISCOUNT:

\* It is the type of discount that is offered by the seller to the buyer as a reduction in the price of the product to ensure bulk sales at the time the purchase is made.

\* It is allowed for both cash & credit transactions.

## ii) CASH DISCOUNT:

- \* It is offered by the seller to the buyer on the invoice amount at the time of making payment within the stipulated time to ensure prompt payment for the items purchased.
- \* It is allowed only for cash transactions.

[NOTE - Trade discount should not be entered in the books of accounts]

## TRIPLE COLUMN CASH BOOK:

- \* Triple column cash book has three amount columns namely cash column, discount columns and bank column.
- \* Triple column cash book involves contra entry.
- \* When bank and cash account are involved in a journal entry, it is called contra (opposite) entry.

## MODERN RULES OF ACCOUNTING:

	INCREASE	DECREASE
ASSETS	Debit	Credit
LIABILITIES	Credit	Debit
INCOME	Credit	Debit
EXPENSES	Debit	Credit
CAPITAL	Credit	Debit

## ENDORSEMENT:

\* For example, 'X' is our debtor and 'Y' is our creditor.

\* Now, 'X' paid a cheque amounting to ₹50,000 and we endorse the cheque to 'Y'.

\* This is called endorsement.

CARD

## ACCOUNTING FOR CREDIT/DEBIT SALE:

1. Bank a/c                      Dr

To sales a/c

[Sales made through debit / credit card]

2. Purchase a/c                      Dr

To bank a/c

[Purchase made through debit / credit card]

3. Commission a/c Dr  
 To bank a/c  
 [Commission charged by bank]

[NOTE: Bank charges commission for collecting amount from debit/credit card]

SOME EXAMPLES OF PERSONAL REPRESENTATIVE ACCOUNT:

LIABILITY	ASSET
* Outstanding expenses a/c	* Expenses paid in advance a/c
* Expenses payable a/c	* Unexpired <del>expired</del> expense
* Expenses due a/c	* Unaccrued expenses
* Expenses unpaid a/c	* Prepaid expenses a/c
* Expenses accrued but not paid a/c	
ASSET	LIABILITY
* Outstanding income a/c	* Income received in advance
* Income receivable	* Pre received income a/c
* Income accrued but not received a/c	* Unexpired income a/c
* Income received but not received a/c	* Unaccrued income a/c



## SOME EXAMPLES OF ASSETS:

- \* Cash
- \* Bank
- \* Debtors
- \* Stock of raw materials
- \* Stock of
- \* Stock of firms
- \* Stock in trade
- \* Opening stock
- \* Closing stock
- \* Loose tools
- \* Machinery
- \* Plant & machinery
- \* Vehicles
- \* Computers
- \* Computer software
- \* Copy rights
- \* Patent right
- \* Trademark
- \* Goodwill
- \* License
- \* Land
- \* Building
- \* Investment

- \* Property
- \* Livestock
- \* Agricultural product
- \* Pig
- \* Goat
- \* Elephant
- \* Cow
- \* Loan advanced
- \* Bills receivable
- \* Fixed deposit with bank
- \* Prepaid rent
- \* Interest accrued on investment
- \* Life insurance premium paid
- \* Personal income tax paid
- \* Household expenses paid
- \* Drawings by cash
- \* Drawings by goods
- \* Building under construction
- \* Capital work in progress
- \* Provision for bad & doubtful debts. [conceptually assets, technically liability]
- \* Provision for discount on debtors
- \* Provision for depreciation
- \* Investment fluctuation reserve etc.

- \* Suspense a/c Dr.
- \* Telephone deposit
- \* EB deposit
- \* Security deposit
- \* Rental deposit
- \* Stock of stationery
- \* Wages on erection on machinery.
- \* Installation charges for assets
- \* Import duty on purchase of assets.
- \* Freight charges on purchase of assets.
- \* Commission charges on purchase of assets.
- \* Mutual funds
- \* Jewellery.
- \* Bullion
- \* Trade receivables
- \* Purchase of grass.

#### SOME EXAMPLES OF LIABILITIES:

- \* Creditors
- \* Loan borrowed
- \* Bills payable
- \* Provision for taxation [Estimated tax liability]
- \* Tax payable [Actual tax liability]
- \* Bank overdraft

- \* Cash credit
- \* Salary payable
- \* Royalty received in advance.
- \* Capital contributed
- \* Provision in discount for creditors.
- \* Provision for damages.
- \* Provision for warranty.
- \* General reserve a/c
- \* Investment fluctuation reserve a/c
- \* Dividend equalisation reserve a/c
- \* Worksmen compensation a/c
- \* Contingency reserve a/c
- \* Equity share capital a/c
- \* Preference share capital
- \* Debentures
- \* Suspense a/c credit
- \* Outstanding wages.
- \* Outstanding interest.
- \* Commission received in advance.
- \* Works manager's outstanding commission.
- \* General manager's outstanding commission.
- \* Apprenticeship premium received in advance.
- \* Outstanding salary.
- \* Outstanding office expenses.

## SOME EXAMPLES OF INCOMES:

- \* Interest received.
- \* Donation received.
- \* Income from investment.
- \* Bad debts recovered.
- \* Sundry creditors written back [not paying credit]
- \* Miscellaneous income.
- \* Scrap value realised on abnormal loss.
- \* Insurance compensation received in respect of abnormal loss.
- \* Scrap value realised on normal loss.
- \* Sale of by product.
- \* Sales net.
- \* Profit on sale of asset.
- \* Profit on sale of investment.
- \* Share transferred fee received.
- \* Discount received from customers.
- \* Till takings.
- \* Dividend from investments.
- \* Interest on drawings.
- \* Commission received.
- \* Rent received.
- \* Apprenticeship premium.
- \* Royalty received.

## SOME EXAMPLES OF EXPENSES:

- \* Salary
- \* Rent paid
- \* Telephone charges
- \* Royalty paid
- \* Interest paid
- \* Wages [Loading & unloading charges]
- \* Freight inward [Relating to purchase - Direct expense]
- \* Freight outward [Air, water, lorry, railway] [Relating to sale - Indirect expense]
- \* Carriage inward [Freight and carriage means transport]
- \* Carriage outward
- \* Donation paid
- \* Subscription paid
- \* Bad debts
- \* Insurance paid
- \* Miscellaneous expenses.
- \* Abnormal loss
- \* Normal loss
- \* Shifting expenses a/c.
- \* Free sample given to customers.
- \* Gift given to employees
- \* Purchase
- \* Loss on sale of asset.
- \* Loss on sale of investment.

- \* Underwriting commission
- \* Preliminary expenses
- \* Expenses on issue of shares
- \* Discount allowed to customers
- \* Depreciation
- \* Ammortaition
- \* Depreciation on tangible assets
- \* Ammortaition on intangible assets
- \* Innaguration expenses a/c
- \* Advertisement expenses a/c
- \* Distribution expenses
- \* Warehouse charges
- \* Delivery charges
- \* Commission on sales
- \* Commission on purchases
- \* Octroi duty. [Duty on purchase - some states have octroi duty - when our goods enter into that states port, we have to pay octroi duty]
- \* Import duty.
- \* Clearing charges [Expense made to clear goods from port]
- \* Dock used
- \* Transport charges
- \* Travelling expenses
- \* Printing & stationery
- \* Stationery consumed
- \* Sales promotion

- \* Directors fee
- \* Directors remuneration
- \* Perquisite to employees
- \* Repairs & maintenance
- \* General charges
- \* Electric charges
- \* Interest on loans
- \* Interest on capital
- \* Repairs to factory
- \* Rents & rates & taxes
- \* Insurance
- \* Interest on bank overdraft
- \* Establishment expenses
- \* Postage
- \* Bank charges