Chapter 2 Basic Accounting Terms

Short Question for Basic Accounting Terms

Question 1

Define basic accounting terms.

Answer: Basic accounting terms refers to the accounting terms that are used daily in the world of business.

Question 2

Give three examples of revenues.

Answer: The three examples of revenues are

(i) Amount received from the sale of goods

(ii) Amount received from providing service to customers

(iii) Receipts of commission, interest, rent, etc.

Question 3

Distinguish between profit and gain

Answer: Profit is the excess of revenues over expenses during an accounting period. It is the result of business transactions which are of regular nature whereas gain arises from events or transactions which are incidental to business such as a sale of a fixed asset or winning a lottery prize.

Question 4

Distinguish between fixed assets and current assets

Answer: Fixed assets refer to those assets which are held for continued use in the business and are not meant for resale whereas current assets are either meant for sale or which are expected to be converted into cash within one year.

Question 5

Distinguish between revenue expenditure and capital expenditure

Answer: If the benefit of an expenditure is exhausted within a year, it is treated as revenue expenditure (also called expense). On the other hand, if the benefit of expenditure lasts for more than a year it is treated as capita;l expenditure (also called an asset).

Question 6

Distinguish between expense and expenditure

Answer: Expense is the cost incurred in producing and selling goods and services. Thus, it includes the cost of goods sold and the amount paid for salaries, rent, commission, etc. On the other hand, expenditure is a wider term which includes expense also. Expenditure is the amount spent on acquiring assets, goods, and services.

Question 7

Distinguish between expenses and losses.

Answer: If the benefit of expenditure is exhausted within a year it is called expense, whereas, excess of expenses of a period over its related revenues is termed as a loss.

Question 8

Give two characteristics of a business transaction.

Answer: The two characteristics of a business transaction are.

(i) It results in a change in the financial position of the firm,i.e. A change in the values of some of the assets, liabilities or capital.

(ii) The change must be capable of being expressed in terms of money.

Very Short Question for Basic Accounting Terms

Question 1

What is Capital?

Answer: It refers to the amount invested by the proprietor in a business enterprise. It can be expressed as Capital = Assets – External Liabilities

Question 2

What are Drawings?

Answer: Drawings refers to any cash or value of goods withdrawn by the owner for personal use.

Question 3

What are Liabilities?

Answer: It refers to the amount which the firm owes to outsiders (expecting the amount owed to the proprietor).

Question 4

What are Assets?

Answer: Assets are valuable resources owned by a business enterprise which can be measured in terms of money.

Question 5

What are the Current Assets?

Answer: Current assets include cash and other assets which are expected to be converted into cash within a short period(normally within one year).

Question 6

Give two examples of current assets.

Answer: The two examples of current assets are cash and stock.

Question 7

Give two examples of tangible assets.

Answer: The two examples of tangible assets are land and building and stock

Question 8

Give two examples of intangible assets.

Answer: The two examples of intangible assets are goodwill and prepaid expense

Question 9

What are fictitious assets?

Answer: These are the assets which cannot be realised in cash or no further benefit can be derived from those assets. Such assets include a debit balance of profit and loss A/c and the expenditure not yet written off such as advertising expenses etc.

Question 10

What are the current liabilities?

Answer: Current liabilities refer to those liabilities which are to be paid in the near future(normally within one year)

Question 11

Give two examples of current liabilities.

Answer: The two examples of current liabilities are creditors and bill payable.

Question 12

What are the internal liabilities?

Answer: All amounts which a business entity has to pay to the proprietor or owners are internal liabilities such as capital and accumulated profits.

Question 13

What is the expense?

Answer: Expense is the cost incurred in producing and selling goods and services.

Question 14

What are the revenue?

Answer: Revenue is the income of a recurring (regular) nature such as receipts from the sale of goods, rent, commission, etc.

Question 15

What is income?

Answer: Excess of revenue over expenses is called income. Income = Revenue – Expenses.

Question 16

What is a voucher?

Answer: A voucher is a document on the basis of which transactions are first recorded in the book.

Question 17

What is a trade discount?

Answer: When a discount is allowed by a seller to its customers at a fixed percentage on the list or catalogue price of the goods it is called a trade discount. It is not recorded in the books of account.

Question 18

What is a cash discount?

Answer: When a discount is allowed to the customers for making prompt payment it is called cash discount. It is always recorded in the books of account.

Question 19

What is meant by purchases?

Answer: The term purchases are used for buying of goods for resale or for use in the manufacturing process. The term purchases included both cash and credit purchase of goods.

Question 20

What is meant by sales?

Answer: The term sales is used for the amount of the sale of goods and services rendered. The term sales include both cash and credit sales.

Question 21

Define merchandise.

Answer: Merchandise means goods for sale.

Question 22

Profit is earned on the sale of a fixed asset. What should be the accounting treatment of this profit?

Answer: It is a capital profit. Hence, it should be transferred to the capital reserve.

Question 23

Give two examples of revenue expenditure.

Answer: The two examples of revenue expenditure are the cost of goods sold and salary.

Higher Order Thinking Skills (HOTS) Questions

Question 1

Godrej Ltd. imported from Germany one machinery for sale in India and other machinery for production purposes. Will you treat them goods or fixed assets?

Answer: The first machinery will be treated as goods, and secondary machinery will be treated as fixed asset.

Question 2

Mr. Jaspal Singh dealing in electronic goods sold 10 TV sets costing ₹30,000 each at ₹40,000 each. Out of this ₹, 5,00,000 were received in cash and the balance is not yet received. State the amount of revenue.

Answer: Revenue will be ₹8,00,000(i.e 20TV sets X ₹40,000) Revenue is the amount either received or receivable from sale of goods and services. Both cash sales and credit sales are included in revenue.

Question 3

Mr. Dinanath who owed us ₹50,000 became insolvent and paid only 40% of this amount. What is the term used for the amount not received?

Answer: Bad debts.

Question 4

Explain a few basic accounting terms.

Answer: Few basic accounting terms are.

- **Business Transaction- Any economic activity that changes the financial position of a company is known as a business transaction. A few features of a business transaction are.**

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        - It includes all the economic activities of a company. All goods or services that are purchased and sold for cash or credit, employee salaries, interest on borrowed money, etc, are few examples of a business transaction.
        - Transactions are divided into two parts, external and internal. The external transactions are those transactions that are made between two businesses. Such as the purchase of goods and services. Internal are those economic activities that have taken place within the organization.
        - This transaction changes the financial status of a company.

- **Events- An event is defined as the result or the outcomes of a transaction. Examples of events are. Rahul starts a business with a capital of ₹5,00,000. He purchases products for ₹4,00,000 for cash and sells 3/4th of these goods for 3,80,000. He also pays ₹20,000 as the rent of the godown. The following results can be outlined from the above transactions.**

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        - ₹5,00,000 of investment for the business
        - Goods purchased ₹4,00,000
        - Cash sales ₹3,80,000
        - Godown payment ₹20,000

- **Account- An account is a place where all the transactions of a person or a business are recorded. For each asset, liabilities, expenses or income separate account is maintained.**

- **Capital-** It is the total amount invested by the owner or proprietor in a business. This amount can be in the form of goods, assets, and cash, which is used in the purchase of goods and assets. Capital can be derived by Capital=Assets-Liabilities

- **Drawing-** All the cash or cost of goods withdrawn by the owner for his/her personal use in known as drawings

- **Liability-** This particular amount is the amount which the company owes to the external or another firm. Liabilities can be expressed as Liabilities= Assets-Capital.

- **Assets-** Asset is something that is owned by the company including the due amount from other companies or debtors.

Value-Based Questions

Question 1

What is the value involved in classifying the assets into current and non-current?

Answer: Classification of assets into current and non-asset helps in ascertaining the liquidity position of the business entity. Non-current assets are held for continued use in the business whereas current assets are expected to be converted into cash within one year.

Question 2

Discuss the value involved in classifying the receipts into capital and revenue?

Answer: Classification of receipts into capital receipts and revenue receipts is essential for the preparation of financial statements since revenue receipts are shown on the credit side of trading and profit and loss account whereas capital receipts are shown in the balance sheet.

Question 3

Identify the value involved in classifying the expenditure into capital and revenue.

Answer: Financial statements cannot be prepared without classifying the expenditure into capital and revenue. Capital expenditure is written in the balance sheet whereas revenue expenditure is written on the debit side of trading or profit and loss account.

Question 4

What is the reason that the capital expenditure is shown in the balance sheet?

Answer: Amount spent on acquiring or erection of fixed assets is termed as capital expenditure. Such expenditure is shown in the assets because it yields benefit over a long period of time.