

Chapter 4 Process and Bases of Accounting

Question 1

Define Process of Accounting

Answer- Accounting process of a company starts with the identification of the company's transaction and then recording, categorizing, and summarizing of a business transaction, which helps in preparation of trial balance and financial statement.

Question 2

What is the cash basis of accounting?

Answer- In cash basis of accounting, incomes are not recorded unless they are received in cash. Similarly, expenses are recorded only when they are paid in cash.

Question 3

What is accrual basis of accounting?

Answer- In this process, incomes are registered when it is accrued or earned, whether the cash is collected or not, for instance, for a sales done on credit will be registered in the total sales of the term. Likewise, expenses are registered when it becomes due or incurred and not when the cash is paid for them.

Question 4

In which basis of accounting outstanding expenses are not recorded?

Answer- In cash basis of accounting the outstanding expenses are not recorded.

Question 5

Write two advantages of accrual basis of accounting.

Answer- The two advantages of accrual basis of accounting are.

- (i) It reveals true profit or loss for a specific period.
- (ii) It adheres to the matching principle of accounting.

Question 6

Which basis of accounting is recognized under the Companies Act, 2013.

Answer- The accrual basis of accounting is recognized under the Companies Act, 2013

Question 7

Does the cash basis of accounting violate GAAP? IF, yes, how?

Answer- Yes, the cash basis of accounting violates GAAP because it does not follow the principle and accrual concept.

Question 8

Explain in details all the steps followed in the process of accounting.

Answer- The steps included in the process of accounting are.

- **Identification of Transaction-** Accounting only deals with monetary transaction. Any event that cannot be measured in terms of money cannot be accounted for in accounting. For all the monetary transaction it is important to have a voucher or an invoice as a piece of evidence. The evidence of the transaction is known as a source document.
- **Preparation of Voucher-** According to the source document entry, first the transaction is recorded in a voucher, later from the voucher it is transferred to journal or original book of entry.
- **Recording in books of original entry-** The book in which the transaction is entered for the first time from a voucher or the source document is known as a book of original entry. Example of an original book of entry is Journal.
- **Posting of Ledger-** Once the transaction is recorded in the journal, it is then entered into the ledger. The ledger is a book of account where all the transactions are recorded according to its nature.
- **Preparation of Trial Balance and Financial Statement-** The final step of the accounting process in the preparation of trial balance and financial statement. The final balance of the ledger account helps the management to prepare the trial balance and financial statement. Trial balance is structured with the help of debit and credit balance of ledger account to verify the accuracy of the posting and balancing of the ledger account. All the balances recorded in the trial balance on the basis of ledger provides a base for preparing the financial statement of a company.