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| 1 | <p>i. What relationship exist between the position of an account on the balance sheet and the rules for recording increase in that account.</p> <p>ii. What requirement is imposed by the double entry system in the recording of any business transaction?</p> |
|---|---|

Ans.

i.

Assets are located on the left side of the balance sheet equation; an increase in an asset account is recorded by an entry on the left (or debit) side of the account. Liabilities and owners' equity are located on the right side of the balance sheet equation; an increase in a liability account or an owners' equity account is recorded by an entry on the right (or credit) side of the account.

Although it has no obligation to issue financial statements to creditors or investors, Baker Construction still should maintain an accounting system. For a start, the company probably has numerous reporting obligations other than financial statements. These include income tax returns, payroll tax returns, (including workers' compensation insurance) and payroll data, which must be reported to individual employees.

Even though the company is not required by law to issue financial statements, Tom Baker should find such statements useful in managing the business and also in arranging financing should the business ever need additional capital.

In addition, an accounting system provides managers and employees with a wealth of information vital to daily business operations. For example, the system keeps track of the amounts due from customers and amounts payable to employees, tax authorities, and suppliers. It also provides information about the company's cash position and the performance of different departments within the organization. Another important use of an accounting system is establishing the accountability of specific employees for the assets and operations under their direct control.

If the account is an asset account, all asset accounts usually have debit balances, in order to record an increase the account needs to be debited.

The balance sheet, sometimes called the statement of financial position, lists the company's assets, liabilities, and stockholders' equity (including dollar amounts) as of a specific moment in time. That specific moment is the close of business on the date of the balance sheet. A balance sheet is like a photograph; it captures the financial position of a company at a particular point in time. The other two statements are for a period of time. As you study about the assets, liabilities, and stockholders' equity contained in a balance sheet, you will understand why this financial statement provides information about the solvency of the business.

The balance sheet is a formal document that follows a standard accounting format showing the same categories of assets and liabilities regardless of the size or nature of the business. Accounting is considered the language of business because its concepts are time-tested and standardized. Even if you do not utilize the services of a certified public accountant, you or your bookkeeper can adopt certain generally accepted accounting principles (GAAP) to develop financial statements.

The strength of GAAP is the reliability of company data from one accounting period to another and the ability to compare the financial statements of different companies.

ii. What requirement is imposed by the double entry system in the recording of any business transaction?

Companies record every transaction in their accounting books based on the double-entry system. Because every transaction involves certain kinds of monetary exchanges between at least two business accounts, the term "double-entry system" refers to the dual entries companies record into the pairs of accounts. Depending on the transaction, the value of each of the accounts increases or decreases. To increase or decrease an account, companies make a debit or credit entry to the account based on the account type. The essential point of the double-entry system is to achieve a recording balance between related accounts.\

Transaction and Accounts

A business transaction can be anything involving an income statement account and a balance sheet account, or solely balance sheet accounts. To use the double-entry system of accounting, companies must first determine the transaction and identify the related accounts. Companies may carry out transactions that are revenue or expense related, and transactions that associate with assets, liabilities or equity. Thus, companies also group transaction accounts into accounts for revenues and gains, expenses and losses, assets, liabilities and equity.

Increase or Decrease

To record a business transaction, companies must ascertain whether the transaction has caused each of the related accounts to increase or decrease. A transaction may cause all related accounts to increase or decrease at the same time or can result in one account increasing while the other account decreases. For example, a cash sale transaction involves the revenue account and the cash account, which is an asset account, and makes both the revenue account and the cash asset account increase at the same time.

Debit and Credit

Debit and credit in accounting recording are not what they mean in the area of money and finance, but rather designations for different accounts and descriptions of any account changes in balances. The accounting recording system assigns all asset, expense and loss accounts as debit accounts and all liability, equity, revenue and gain accounts as credit accounts. A debit made to a debit account and a credit made to a credit account increase the balance of the respective accounts. On the contrary, a credit made to a debit account and a debit made to a credit account decrease the balance of the respective accounts.

Balance Between Accounts

The double-entry recording system always results in an equal amount recorded in the related accounts in the form of a debit entry and a credit entry. While a debit represents the money used in a transaction, a credit indicates the money source for the transaction. A company may make a debit entry to a debit account to show an increase for the account or make a debit entry to a credit account to register a decrease for the account. On the other hand, a company may make a credit entry to a debit account to display a decrease for the account or make credit entry to a credit account to demonstrate an increase for the account. For example, in a cash sale transaction using the double-entry system, a company makes a debit to the cash asset account, which is a debit account, to increase the amount of cash received from the sale, and makes a credit for the same amount to the revenue account, which is a credit account, to increase the amount of revenue as a result of the sale.

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| 2 | <p>i. What factor should be considered when comparing the net income figure of a partnership to that of a corporation of similar size?</p> <p>ii. What do you understand the concept and meaning of amalgamation?</p> |
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Ans.

i.

In a partnership, it is the residual profit which is divided between the partners in the profit and loss sharing ratio. The residual profit is the amount of profit remaining after taking into account the fact that the partners will be entitled to a proportion of the profit under the terms of the partnership agreement. These proportions are the 'appropriations of profit'. They will arise because of a variety of factors. For example, the partners may have differing degrees of involvement, or may bring specific skills to the business.

However, these reasons are rarely an issue in exam questions. It is more likely that exam questions will require candidates to calculate and account for appropriations of profit according to the terms of the partnership agreement. A key point to remember is that as in a sole trader's accounts, any amounts actually paid to the owners (whether in cash or in kind) should be treated as drawings.

If a partner is entitled to a salary, it is dealt with as part of the appropriation of profit. It is not an expense of the business, and should not be charged to the income statement in order to calculate profit. Only salaries paid to employees of the business are charged to the income statement.

Partners' capital and current accounts

While it is normally the case that all appropriations of profit are taken to a current account, it is important to be clear about whether the question requires this approach. If so, this may be referred to by stating that the partnership maintains fixed capital accounts. This means that each partner will have a capital account and a current account. The capital account will record the initial introduction of capital, and will normally only be adjusted if the partner introduces additional capital. The current account will record the appropriations of profit and drawings. If the partnership maintains floating capital accounts, there will be no current account, and appropriations of profit and drawings will be recorded in the capital account.

Amalgamation is a way to acquire cash resources, eliminate competition, save on taxes, or influence the economies of large-scale operations. Amalgamation may also increase shareholder value, reduce risk by [diversification](#), improve managerial effectiveness, and help achieve company growth and financial gain.

On the other hand, if too much competition is cut out, amalgamation may lead to a monopoly, which can be troublesome for consumers and the marketplace. It may also lead to the reduction of the new company's workforce as some jobs are duplicated and therefore make some employees obsolete. It also increases debt: by merging the two companies together, the new entity assumes the liabilities of both.

Amalgamation Procedure

The terms of amalgamation are finalized by the board of directors of each company. The plan is prepared and submitted for approval. For instance, the High Court and Securities and Exchange Board of India (SEBI) must approve the shareholders of the new company when a plan is submitted.¹

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| 3 | <p>You are employed by a business consulting firm as an information system specialist. you have just begun an assignment with a startup company and have been given the assignment of discussing with the owner her need for an accounting system. How would you respond to the following questions from the owner?</p> <ol style="list-style-type: none">Who designs and install accounting system?What is the purpose of an accounting system and what are its basic functions?How does management s explanation enhance the usefulness of financial accounting information? |
|---|--|

Ans.

(A)

Nothing could make a business more vulnerable than a weak and porous system of accounting. We simply carryout a preliminary study of our client's business management process (BMP) and thereafter design a system that adequately captures all the intricacies of financial transactions and controls. In recommending a system and perhaps a complimentary application package, we consider such things as nature of business, volume of transactions and workflows. At each stage of the design and implementation, we carry along the client for input and modifications that are indispensable in a robust but tailor made system. In the end, our client's satisfaction and efficiency is priority.

Businesses typically computerize an accounting information system in all but the smallest organizations. Computer users enter data into software programs that complete the calculations and classify and file the entries into the proper categories. The system can then generate various types of reports, depending on the user's request. The information system includes all steps in the accounting cycle, and hard-copy paperwork that proves the transactions, such as work orders, invoices and financial statements becomes part of the system. In smaller businesses, such as a mom-and-pop operation where few transactions occur, the business may maintain the accounting information system manually. Again, the bookkeeper uses the entire accounting cycle and constructs manual reports from the results.

(C)
Managerial accounting is the practice of identifying, measuring, analyzing, interpreting, and communicating financial information to managers for the pursuit of an organization's goals. It varies from financial accounting because the intended purpose of managerial accounting is to assist users internal to the company in making well-informed business decisions.

How Managerial Accounting Works

Managerial accounting encompasses many facets of accounting aimed at improving the quality of information delivered to management about business operation metrics. Managerial accountants use information relating to the cost and sales revenue of goods and services generated by the company. Cost accounting is a large subset of managerial accounting that specifically focuses on capturing a company's total costs of production by assessing the variable costs of each step of production, as well as fixed costs. It allows businesses to identify and reduce unnecessary spending and maximize profits.

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