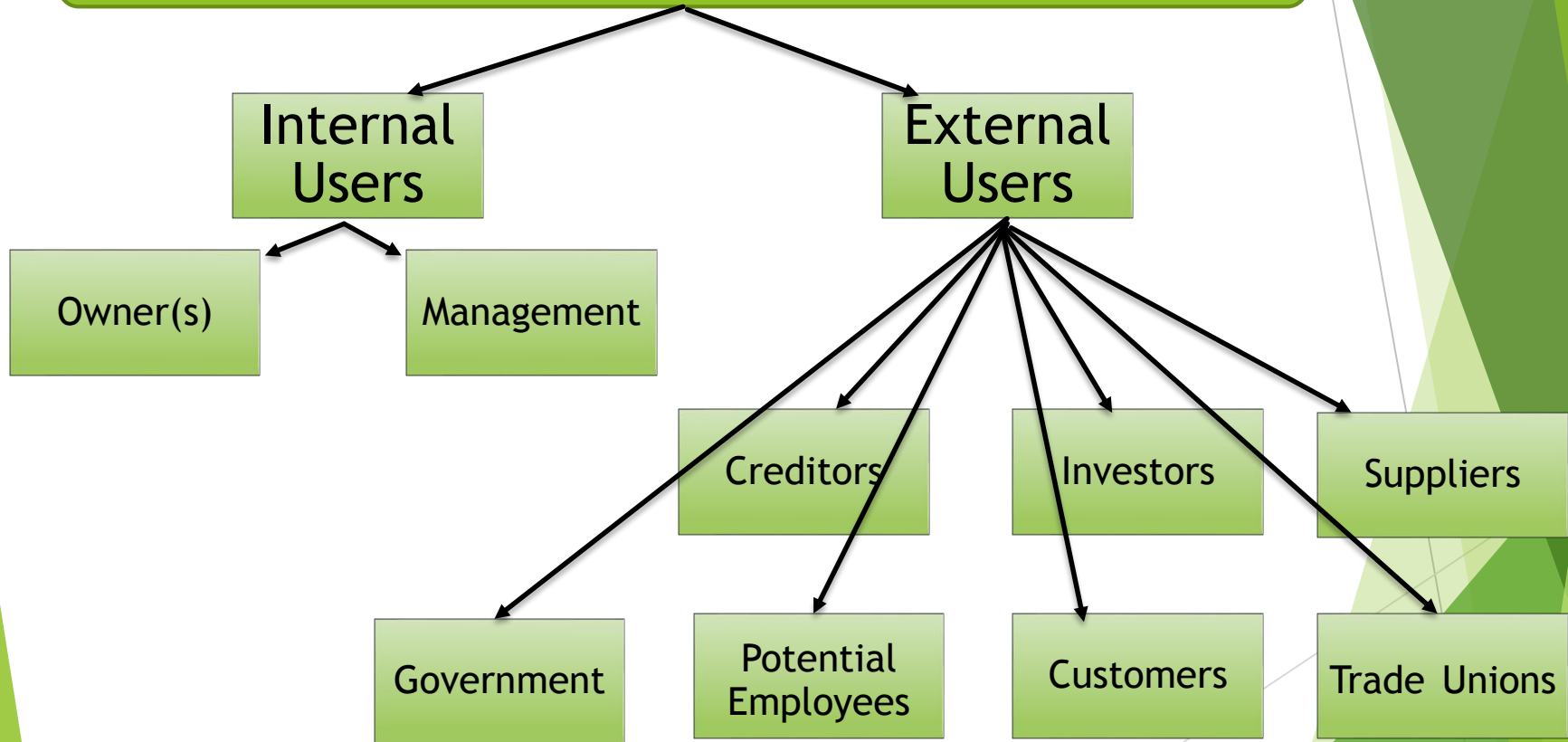


Fundamentals of Financial Accounting-**FFA**

Operational Level 1-OL1

Accounting with Jaweed Hassan-ACMA,MBA

Users of Accounting Information



Why do “Users of Accounting Information” need information about business entity?

```
graph TD; A[Why do “Users of Accounting Information” need information about business entity?] --> B[To know about “Profitability” of the entity]; A --> C[To know about “Solvency” of the entity]; A --> D[To know about “Liquidity” of the entity];
```

To know about
“Profitability”
of the entity

To know about
“Solvency” of
the entity

To know about
“Liquidity” of
the entity

Accounting- *“The Language of Business”*

“Accounting is the art of **interpreting**, **measuring**, **recording** and **communicating** the results of economic activities”.

Purpose of Accounting:

1. Maintaining Information
2. Using Information
3. Providing Information

Language: The medium by which information is communicated to another.

Business: Any activity undertaken with the objective of earning profit.

Classification of Business

“Business can be classified as follows:

1. Activity-wise Classification
2. Ownership-wise Classification

Classification of Business Activity-wise			
S.no	Servicing Business	Trading/Merchandising Business	Manufacturing Business
1.Purpose	Profit Earning	Profit Earning	Profit Earning
2.Function	Services are sold .	Goods are purchased in reade-to-sale condition and sold .	Raw material is purchased , converted into finished goods and sold .

Inventory/Goods/Stock/Merchandise

Anything purchased for resale.

Classification of Business Ownership-wise

S.No	Sole-Proprietorship	Partnership	Joint Stock Company/Company/Corporation
1.Quantity of Owners	Single Owner	Banking Business: 2 to 10 Other than Banking: 2 to 20	Single Member Co:1 General Private Company: 2 to 50 Public Unlisted Company: 3 to ... Public Listed Company: 7 to ...
2.Legal Entity	Legal entity is of owner.	Legal entity is of partners.	Legal entity is of the business.
3.Ownership and Management	Ownership and management may be same.	Ownership and management may be same.	Ownership and management are different.
4.Transfer of Ownership	Transfer of ownership is comparatively difficult.	Transfer of ownership is comparatively difficult.	Transfer of ownership is comparatively easy.
5.Existence	Limited life	Limited life.	Perpetual succession.

Asset

Anything of **value** expressed **in term of money** is “Asset”.

or

Any resource that is **expected** to generate **future economic benefits** is “Asset”.

Kinds of Asset

```
graph TD; A[Kinds of Asset] --> B[Personal Assets]; A --> C[Business Assets];
```

Personal
Assets

Business Assets

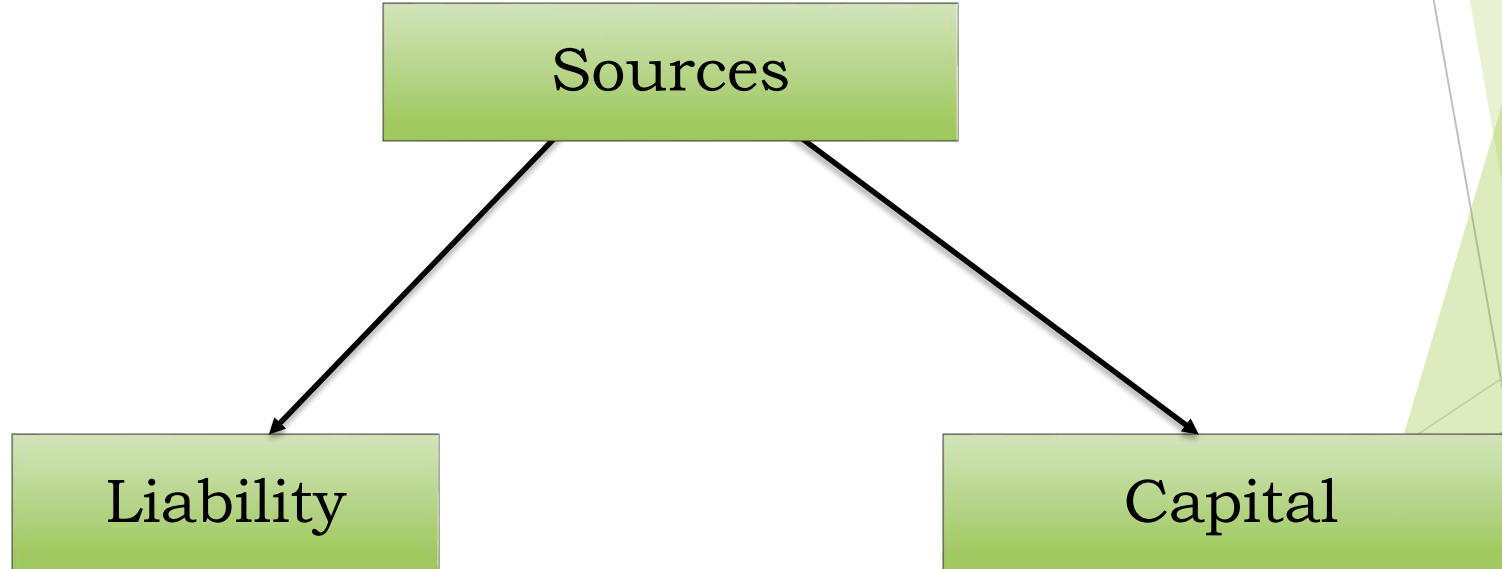
Business Entity Concept

Business entity is an ***economic unit*** that engages in identifiable business activities and is ***separate from the personal affairs of its owners***.

The personal affairs of owners must not be intermingled with business transactions. Otherwise the resulting reports will not be able to describe clearly the financial position and operating results of the business.

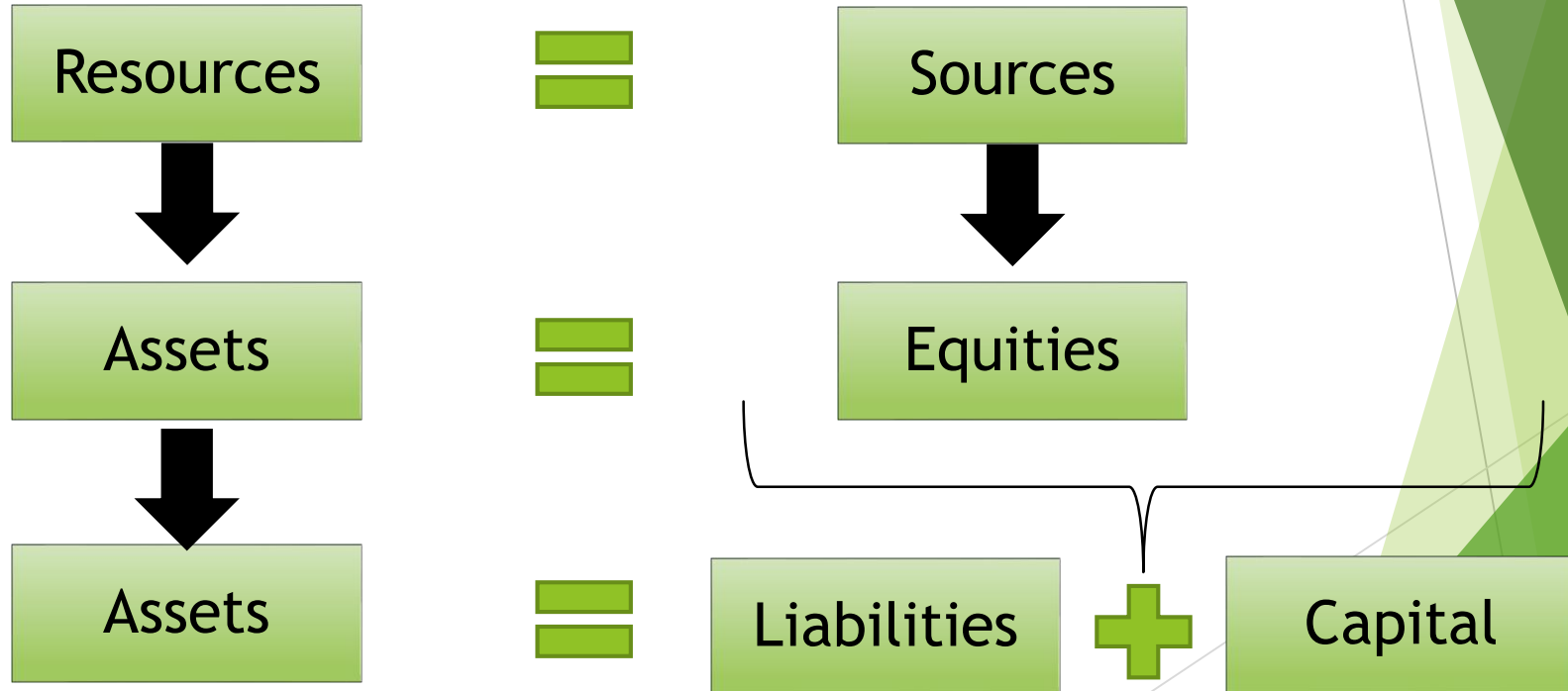
Sources of Resources

Resources mean “Assets”. Whereas sources mean “from where assets have been provided to business”.



S.No	Liability/Outsiders' Equity/External Equity	Capital/Owner's Equity/Proprietorship/Internal Equity/Net Worth/Net Assets
1	Liability means the right/claim of people other than owner in the assets of the business	Capital means the right/ claim of the owner in the assets of the business.
2	Liability means the amount owing to the people other than owner of the business.	Capital means the amount owing to the owner of the business.
3	It is the primary claim on the assets of the business.	It is the residual claim on the assets of the business.

Basic or Fundamental Accounting Equation/Balance Sheet Equation



Basic or Fundamental Accounting Equation/Balance Sheet Equation

Assets

=

Liabilities

+

Capital

Rs.100,000

=

Rs.10,000

+

Rs.90000

Rs.500,000

=

Rs.80,000

+

Rs.420,000

Rs.380,000

=

Rs.100,000

+

Rs.280,000

Which one is right?

Assets

=

Capital

+

Liabilities

Wrong

Assets

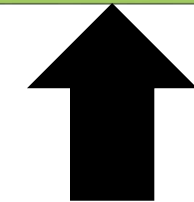
=

Liabilities

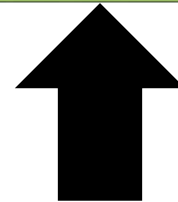
+

Capital

Right



Primary
Claim



Residual
Claim

Cost

Cost of any asset is the “*sum of all payments made or to be made*” to acquire that asset.

Historical Cost Concept:

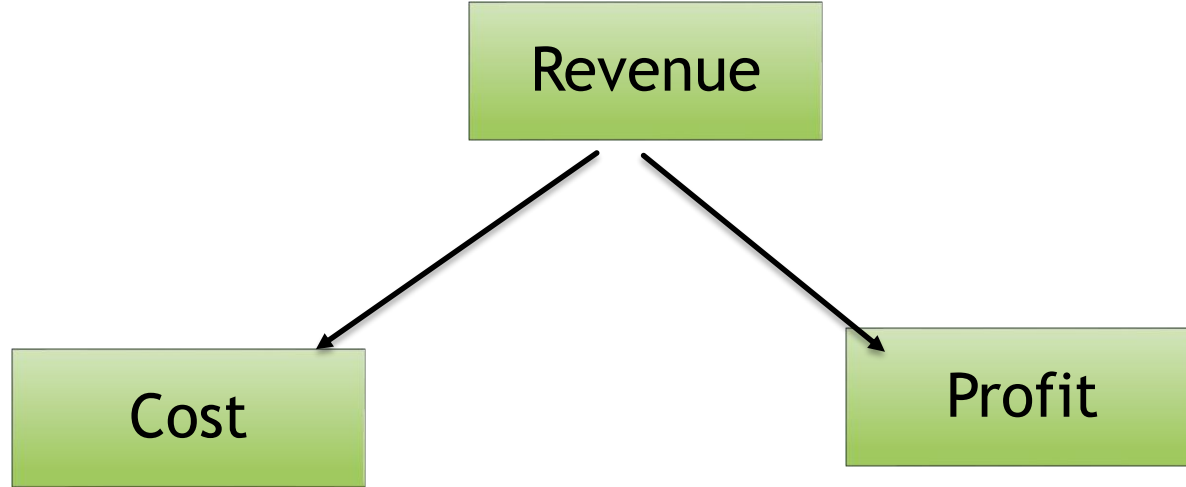
Historical cost concept states that every entity should record its assets at Historical cost.

Historical Cost:

The amount originally paid to acquire any asset is “*Historical Cost*”.

Revenue

The *price* of goods *sold* or services *rendered* is “*Revenue*”.



Profit

Excess amount realized by rendering of services or selling of goods
Is “*Profit*”.

Revenue	=	Cost	+	Profit
Rs.300,000	=	Rs.260,000	+	Rs.40,000
Rs.375,000	=	Rs.315,000	+	Rs.60000
Rs.900,000	=	Rs.700,000	+	Rs.200,000

Revenue = Cost - Loss

Rs.300,000 = Rs.360,000 - Rs(60,000)

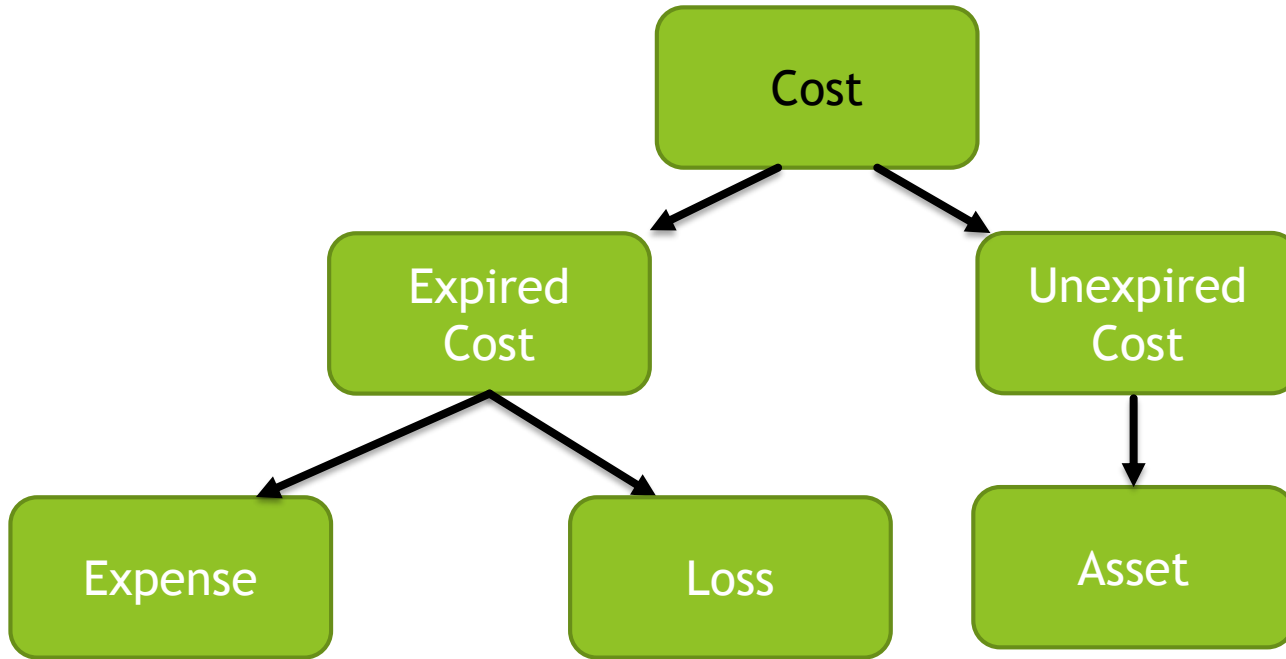
Rs.800,000 = Rs.1,000,000 - Rs.(200,000)

Rs.540,000 = Rs.560,000 - Rs.(20,000)

Expense and Loss

*Cost of goods and services **expired** in the **process of generating Revenue** is 'Expense'.*

*Cost of goods and services **expired** but not generating benefits is 'Loss'.*



Transaction

Any **exchange** of goods or services **expressed in term of money** is 'Transaction'.

Kinds of Transactions

Cash Transaction	Credit Transaction
Any transaction in which immediate payment is made is 'Cash Transaction'.	Any transaction in which immediate payment is not made but is deferred (postponed) to some future date is 'Credit Transaction'.