

# ACCOUNTANCY

## H.S 2nd Year Students

### Unit-I

#### *1. What is not for profit organizations?*

**Ans:** Not for profit organizations are those organizations which are engaged in rendering valuable services to the society or to their members. They are not engaged in buying and selling activities. The primary objective of such organizations is to render services without profit motive.

#### *2. Name two type of non trading organizations having profit motive and two types of organizations having service motive.*

**Ans:** **Non trading organizations having profit motive are-** (a) Firms of practicing chartered accountants and (b) consultant engineers.

**Non trading organizations having service motive are-** (a) Government Educational Institutions, and (b) Government/Charitable Hospitals.

#### *3. What are the objectives of not for profit organizations?*

**Ans:** **The objectives of not for profit organizations without profit motive** are to offer their valuable services for the welfare of the society or for their members by undertaking various promotional activities. **The objectives of not for profit organizations with profit motive** are to earn profit. They earn income by giving some specialized services to the society such as accounting service, legal service, etc.

#### *4. Mention features of not for profit organizations. (1 mark for each point)*

**Ans:** *Features of not for profit organizations are*

- (a) Voluntary Organization:** It is a voluntary association of persons with humanitarian objectives.
- (b) Objective:** Its object is to provide some valuable services to the society or to its members either free of cost or at nominal rates and not to earn profit.
- (c) Sources of funds:** The major sources of fund of such organizations are subscription from their members, donations, financial assistance from Govt., income from investments etc.
- (d) Management:** Such organizations follow the principle of democratic governance. These organizations are usually managed by a managing or executive committee elected by its members.
- (e) Accounts:** These organizations also have to maintain proper accounts to meet the requirements and to exercise proper control over utilization of funds.
- (f) Surplus not distributed among its members:** Unlike other business surplus is not distributed among its members. It is adjusted in the capital fund of such organizations.

**5. Mention the distinctions between profit seeking organizations (trading organizations) and non-profit seeking organizations (non- trading organizations). (1 mark for each point)**

**Ans:** Distinction between profit seeking organizations and non- profit seeking organizations are given below:

Sl no.	Points. of distinction	Trading organizations	Non- trading organizations.
1	Primary activity	Its primary activity is to buy and sell goods.	Its primary activity is to render service for the welfare of the public and its members.
2	Objective	Its object is to earn profit.	Its object is to cater to the needs of its members.
3	Net result of activities	Net result of the activities is called net profit or net loss.	Net result of activities is called surplus or deficit.
4	Financial statements	Financial statements of such organizations include Manufacturing, Trading, Profit and Loss account and Balance Sheet.	Financial statements of such organizations include Receipts and Payments Account, Income and Expenditure account and Balance sheet.

**6. What is Receipts & Payments Account?**

**Ans-** Receipts and Payments Account is merely a summary of cash transactions under proper heads. All receipts are entered on the debit side and all payments are entered on the credit side of the account. It is prepared at the end of the accounting period from the cash book. It generally starts with an opening balance of cash and ends with a closing balance of cash

**7. Why and how is Receipts and Payments Account prepared?**

**Ans-** The Receipts & Payments Account is prepared for the following purposes:

- To inform the members the amount received and spent during a particular period.
- To show a summary of all cash receipts and cash payments at different heads.
- To show the cash position at the end of a period.
- To show the functional activities of an organization.
- To facilitate the preparation of the income and Expenditure Account

**The following is the procedure of preparing a receipts and payments account:**

- Receipts and Payments Account is prepared on the pattern of a cash book.
- This account commences with the opening balance of cash (if any) and opening cash is shown on the debit side of this account as the first item. This account closes with the closing balance of cash at the end of the period which is shown on the credit side as the last item.
- All cash receipts are recorded on the debit side and all cash payments are recorded on the credit side of the account. The balancing figure of this account indicates closing cash.

**8. What are the objectives of preparing Receipts & Payments Account?**

**Ans.** The objectives of preparing Receipts & Payments Account are as follows:

**(i) Summary of Receipts and Payments:** it shows a summary of all cash receipts on different sources and cash payments at different heads.

**(ii) Cash position:** It shows the cash position at the end of a period.

(iii) **Functional activities:** It shows the functional activities of an organization

(iv) **Preparation of income statement:** It facilitates the preparation of the income and Expenditure Account

#### 9. Mention features of Receipts and Payments Account.

**Ans-The features of Receipts and Payments Account are:**

(i) **Summary of Cash Transactions:** It is known as cash book summary for the not for profit organization because it records all cash receipts on the left hand side or debit side and all cash payments on the right hand side or credit side in total under proper heads throughout the year.

(ii) **Items of both revenue and capital nature:** This accounts shows cash transactions of both revenue and capital nature.

(iii) **Avoidance of outstanding items:** Receipts and Payments account does not include any outstanding expenses or incomes.

(iv) **Cash Trial:** Receipts and Payments account is not a trial balance but merely a cash trial.

(v). **Opening and closing balance:** It starts with the beginning cash and bank balance and ends with ending cash and bank balance.

#### 10. Mention two limitations of Receipts and Payments Account.

**Ans: (i) Avoidance of outstanding items:** Receipts and Payments account does not include any outstanding expenses or incomes.

(ii) **Does not show surplus or deficit:** Receipts and Payments account does not show surplus or deficit.

#### 11. What are the basis for preparing Receipts and Payment Account and Income & Expenditure Account?

**Ans:** A Receipts and payment Account can be prepared either from a given cash book; or from the given summary of information from the cash book.

An Income and Expenditure Account can be prepared from a given Receipts and Payment Account.

#### 12. What is Income & Expenditure Account?

**Ans:** Income and Expenditure account is prepared by not-for profit organization. It is prepared to see whether the revenue (incomes) of a particular period is sufficient to cover the expenses (revenue) of that period. Revenue incomes of a particular year are shown on the right hand side and related revenue expenses of that year are shown on the left hand side of this account. The excess of income over expenditure represents surplus while excess of expenditure over income represents deficit. This account is prepared on accrual basis.

#### 13. What are the features of Income and Expenditure Account?

**Ans:** Following are the features of an Income and Expenditure Account:

(i) **Revenue Account:** It is a revenue account.

(ii) **Statement of Incomes and Expenses:** It shows the sources of incomes and heads of expenses relating to a particular period.

(iii) **Basis of accounting:** An Income and Expenditure Account is prepared on accrual basis.

(iv) **Capital Items:** The items of incomes and expenses of capital nature are excluded from recording in this account.

(v) **Placement of Items:** Incomes are shown on the right hand side or credit side and expenses are shown on the left hand side or debit side.

#### 14. Distinguish between Receipts and Payments Account and Income and Expenditure Account.

**Ans:** Following are the points of distinction existing between a Receipt and Payments Account and an Income and Expenditure:

Sl. No.	Points of Distinction	Receipts and Payments Account	Income and Expenditure Account
1.	Form of Account.	It is a summary of cash transactions containing cash receipts on the debit side and cash payments on the credit side.	It is an equivalent to a Profit and Loss Account containing revenue incomes on the credit side and revenue expenses on the debit side.
2.	Objectives	Its objectives are to show cash or bank balance at the end of a period.	Its object is to show surplus or deficit at the end of a period.
3.	Nature of transactions	It contains all cash receipts and cash payments whether revenue or capital nature taken place during a period.	It contains only revenue incomes earned and revenue expenses incurred during a period.
4.	Basis of accounting	It is prepared on cash basis.	It is prepared on accrual basis.
5.	Nature of account	It is a Real Account as it is a summary of cash transactions.	It is a nominal account as it is equivalent to Profit and Loss Account.

#### 15. Distinguish between Profit and Loss Account and Income & Expenditure Account.

Sl. No.	Points of Distinction	Income and Expenditure Account	Profit and Loss Account
1.	Object	It is prepared to find out the surplus or deficit.	It is prepared to find out the profit or loss.
2.	Preparation	It is usually prepared from the Receipts and Payments accounts and adjustments.	It is usually prepared from the trial balance and adjustments.
3.	Organization	It is prepared by not for profit organization.	It is prepared by trading organization

#### 16. What is the meaning of capital receipts and revenue receipts?

**Ans:** Capital receipt means any receipt which can be attributed to any fixed asset/liability account. It includes the receipt of capital, loan, legacies, sale proceeds of fixed assets, etc. They are non-recurring in nature.

**Revenue receipts** are those receipts which can be attributed to any revenue/expense account. It includes the receipt of sale proceeds of goods, rent, interest, commission, etc. They are recurring in nature.

**17. What is the meaning of capital payments and revenue payments?**

**Ans:** Capital Payments are those payments which result in the increase of a fixed assets or decrease in liability. These payments are non-recurring in nature. For examples; Purchase of machinery, furniture etc. Revenue Payments are those payments which are necessary for maintaining the normal activities of the organization. These payments are recurring in nature. For example; purchase of goods for sale, salaries, wages, etc.

**18. Mention two distinctions between capital payments/expenditure and revenue payments/expenditure.**

**Ans:** Following are the distinctions existing between capital payments/expenditure and revenue payments/expenditure:

Sl.No.	Points of Distinction	Capital Payments/Expenditure	Revenue Payments/ Expenditure
1.	Object	It is expenditure for the acquisition of a new asset or for the improvement upon an existing asset.	It is expenditure for maintaining the earning capacity of an organization or for meeting the routine expenses.
2.	Nature	It is non-recurring in nature.	It is recurring in nature.
3.	Duration of benefit	It provides benefit for a longer period extending more than one year.	It provides benefit for a shorter period extending maximum for one year.

**19. Mention two distinctions between capital receipts and revenue receipts.**

**Ans:** Following are the distinctions existing between capital receipts and revenue receipts:

Sl. No.	Points of Distinction	Capital Receipt	Revenue Receipt
1.	Sources of Receipt	Capital receipts do not arise in ordinary course of business. They are non-recurring in nature.	Revenue receipts arise in ordinary course of business. They are recurring in nature.
2.	Utilization	It is utilized for a long term benefit of an organization.	It is used for periodical matching with expenses.
3.	Accounting treatment	Capital receipts are shown in the Balance Sheet.	Revenue receipts are shown in Income and Expenditure Account.

**20. Explain the accounting treatment of the following while preparing Financial Statement (Receipts and Payments Account, Income and Expenditure Account and Balance Sheet) of Not for Profit Organization:**

(a) Life membership fees (b) Legacy (c) Entrance fees (d) Donations (e) Honorarium (f) Sale of old newspapers (g) Sale of old fixed assets (h) Sale of old sports materials (i) Capital Fund (j) Subscriptions (k) Sale of Scrap

**Ans. (a) Life membership fees**

It is a lump sum payment at a time. It is paid by a person to an organization to become member of that organization for the whole life. It is shown on the debit side of the Receipts and Payments Account. It is a capital receipts and while preparing income and expenditure account and Balance Sheet it is shown on the liabilities side of the Balance Sheet.

**(b) Legacy:**

It is a gift made under a will. It may be either in cash or in property. It is non-recurring in nature and is treated as a capital item. If it is received in cash, it is shown on the debit side of the Receipts and Payments Account and as a capital item, it is added to the Capital Fund in the Balance Sheet.

**(c) Entrance fees:**

Entrance fees are received from new members on their admission.

There are two alternatives for accounting treatment of such fees in the absence of any instruction.

**(a) As a non-recurring income:**

Each member pays entrance fees on their admission. So it is non-recurring in nature. Therefore, it may be capitalized and added to the capital fund in the Balance Sheet.

**(b) As a recurring income:**

Every year new members are admitted into an organization and entrance fees are received from them. So it is a recurring in nature in this sense. Therefore, it may be considered as a revenue income and taken to the credit side of the Income and Expenditure Account.

Normally small amount is treated as a revenue income and is taken to the credit side of Income and Expenditure Account and a big amount is treated as capital income and is taken to the capital fund.

**(d) Donations:**

Donation is a gift either in cash or in property made by an individual or an organization without any consideration. It has two accounting treatments.

**(a) Donations for specific purpose:** If donation is received for **specific purpose then** it is a capital receipt and is shown in the liabilities side of the Balance Sheet. It is not shown in the Income & Expenditure Account.

**(b) Donation for general purpose:** If donation is received for **general purpose then** it is a revenue receipt and is shown in the income side of the Income & Expenditure Account.

**(e) Honorarium:**

It is a payment made to a person who is not the regular employee of the organization for a specific service rendered by him to a non-trading organization. For example: Payment to an artist, payment to a lecturer, coach, etc. It is treated as a recurring expense and is shown on the credit side of the Receipts and Payments Account and is debited to the Income and Expenditure Account.

**(f) Sale of old newspapers:**



Non-trading organizations sell their newspapers, journals and periodicals at a nominal value. It is a recurring receipt and hence it is treated as a revenue income and taken to the credit side of the Income and Expenditure Account.

**(g) Sale of old fixed assets:**

Sale of fixed assets has two alternative accounting treatments:

**(a) If the assets sold do not have any book value,** then whole amount received is treated as income and is shown in the income side of the Income & Expenditure Account.

**(b) If the assets sold have any book value,** the whole amount received from sale is compared with its book value. The difference, if any, will be either profit or loss on sale of fixed assets. If there is profit it is shown on the Income side (credit side) of the Income & Expenditure Account. If there is loss then it is shown on the debit side (expenditure) of the Income & Expenditure Account. The book value of the asset sold is deducted from the asset concerned in the balance Sheet.

**(h) Sale of old sports materials:**

The amount received from the sale of old sports materials is a revenue income and is taken to the credit side of the Income and Expenditure Account.

**(i) Capital fund:**

Capital fund is the excess of assets over liabilities of non trading organizations. It is similar to capital account of a trading organization. At the initial stage it is generally created out of special donation received from some donors, from govt. as grants etc. It is shown on the debit side of the Receipts and Payments Account when it is received. It is non-recurring in nature and is treated as a capital income. It is shown on the liabilities side of the Balance Sheet.

**(j) Subscriptions:**

A member is required to pay the amount of money at periodical intervals in order to retain his membership of the organization alive. Such amount of money is termed as subscription. It is a revenue receipts. It is shown in the income side of the income and expenditure account.

**(k) Sale of Scrap:**

The amount realized from sale of scrap is revenue and is shown on the income side of the Income and Expenditure account.

**21. What is the meaning of fund based accounting?**

Not for profit organizations receive funds from its members or non members. Funds should be used for the purpose for which it is collected. For example, a person may donate some money for construction of the Building of the organization. The organization may create this fund named as 'Building Fund.'

Fund based accounting involves preparation of financial statement fund wise and consolidation of those statements to represent the financial position of the organization as a whole. Therefore, the accounting system for which separate fund exists is termed as 'Fund Based Accounting'.

**22. Give three distinctions between Fund Based Accounting and Non Fund Based Accounting?**

Ans:

Points	Fund based accounting	Non fund based accounting
1. Basis of accounting	It is on cash basis	It is on accrual basis
2. Use of funds.	Funds are used for specific purposes except for general fund	Funds can be used for any profit earning purpose.
3. Usual earning	Usually expenditure is more than income, known as deficit.	The result of matching of revenues and expenses either be profit or loss.
4. Accountability	Accountability towards law, regulations, parliament, contributors and donor of funds.	Accountability towards all stakeholders vis owners, creditors, governments, etc.

**23. What is the need for following fund based accounting by a not-for-profit organization?**

Ans: Government and not for profit- organizations are required to organize their accounting system on a fund basis. Fund based accounting involves preparation of financial statements fund wise and consolidation of those statements to represent the financial results as a whole. Particularly, not for profit organizations maintain separate fund for some specific activities of the organization and legally responsible for ensuring that certain funds are used only for such specific purpose for which the same have been contributed by the donors. Hence there is a need maintaining fund based accounting by a not for profit organizations.