

CHAPTER 2 BASIC TERMS

1. Business

Any legal action that is done in order to earn income or profit is called business. It includes the production of goods and services, purchase and sale of goods and services, banking, insurance, education transportation, and any other trading activity etc.

- **Entity:** An economic unit, which may be business entity (enterprise) or non-business entity.
- **Business**

Transaction: A Business transaction is an economic activity of business that changes its financial position. ○ **Account:** It is a record of all business transactions relating to a particular person or item. It is a T-Shaped Performa

2. Trade

Purchase and sale of goods and services in order to earn profit is called trade.

3. Profession

Any work done in order to earn profit which necessarily requires prior training and education is called a profession. For example doctors, lawyers, engineers etc..

4. Proprietor

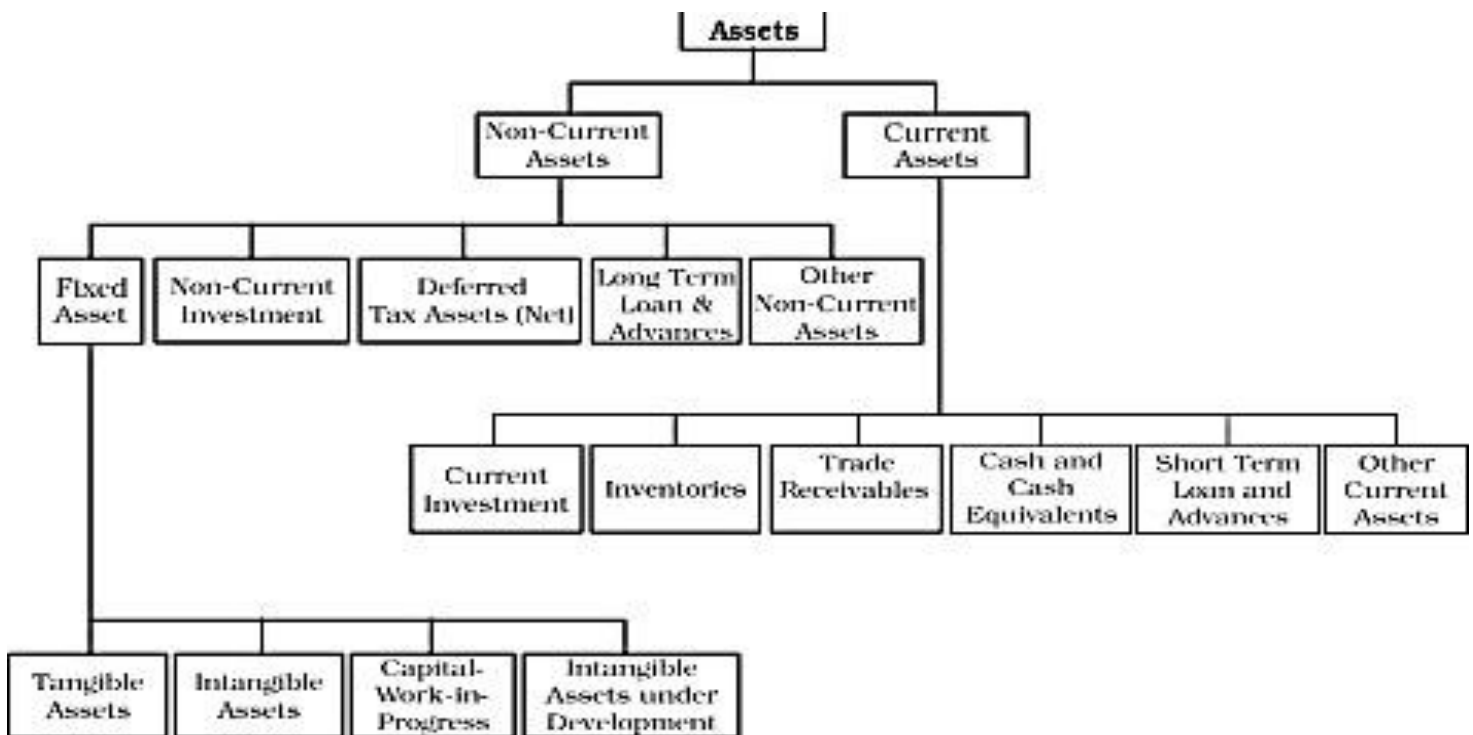
The person who invests capital in the business and entitled to have all profits and losses of the business is called proprietor or owner of the business. The nature of proprietor depends upon the type or nature of the business organization. In a sole trade business, sole trader is a proprietor, in a partnership firm, partners or proprietor and in company shareholders are proprietors.

5. Capital

The amount of cash, goods or assets which is initially invested by proprietor while commencing business is called capital. It is invested to earn profits. In other words, the excess of assets over liability is capital.

6. Assets

All the resources of business having economic value are called assets. These resources help the business to earn a profit and have future value. These are important for running a business and are in the possession of businessman. These are of two types: –



a. Fixed assets

The assets which are used by business for a long time are called fixed assets or non-current assets. These are **continued to be used by the business for a period of more than one year**. For example:- land ,building ,plant, machinery ,furniture ,vehicle etc.

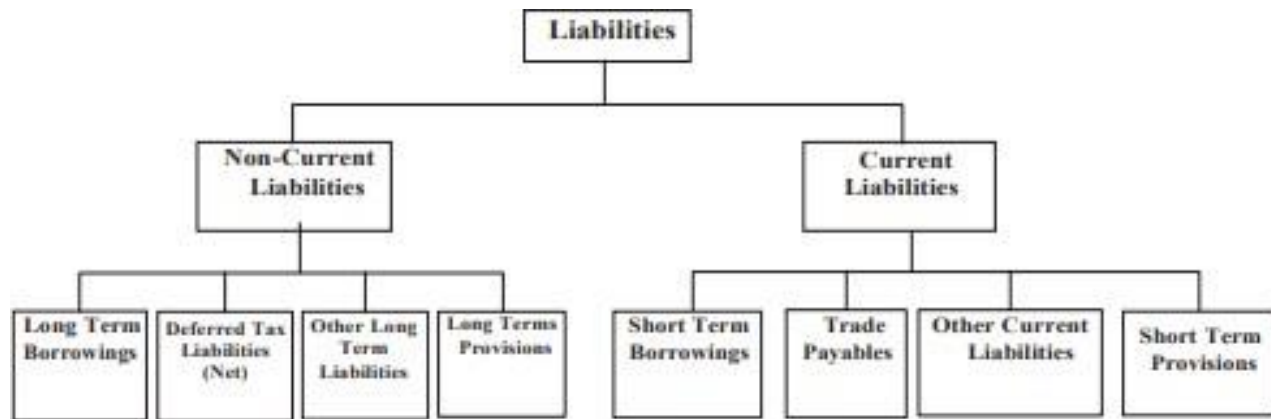
b. Current assets

The assets which are used up in one year or easily get converted into cash in one year are called current assets. For example:- raw material, finished goods, debtors, cash balance and bank balance etc.

7. Liabilities

The amount which business owes to others is called its liabilities. There is a certain amount which business is under obligation to pay.

There are two types of liabilities: –



a. Long-term liabilities (NON CURRENT LIABILITY)

Those liabilities which are usually payable after a period of 1 year. Long-term loans from Financial Institutions, debentures issued by companies etc.

b. Short-term liabilities (CURRENT LIABILITY)

These are those which are payable within one year. For example creditors, bank overdrafts etc.

C. Contingent liability

8. Drawings

The amount of cash or goods which is withdrawn by proprietor from business for its private uses is called drawings. It reduces the capital of the business.

9. Goods

The things which are bought and sold by business are called goods. Goods maybe raw material work in progress of finished goods. In accounting, when goods are purchased it is written as purchases. When goods are sold it is written as sales. It is written as a stock if remain unsold at the end of the year.

10. Purchases

Goods bought for resale are called purchases. This may be in form of raw material or finished goods. Purchase of assets is not called purchases because assets are not purchased for resale.

11. Sales

When purchase goods are sold in order to earn a profit are called sales. When goods are sold for cash it is called cash sales and goods sold on credit are called credit sales.

12. Purchase return

Goods once purchased by the business, are returned back due to any reason is called purchase return or return outwards.

13. Sales return

Goods once sold to the customer when are returned back by them due to any reason then such goods are called as sales returns or return inwards.

14. Stock

These are those goods which are left unsold in the business at the end of the year. The goods unsold at the end of the accounting year are called closing stock. The same stock is called opening stock at the beginning of a new accounting year.

15. Revenue

These are the amount received by a business for selling goods or services. This amount is received from day to day business activity in the form of rent, interest, commission, discount, dividend etc.

16. Expenses

The cost which business incurs for producing goods and services or for using services is called expenses. These include payments

made for wages, salaries, freight, advertisement, rent, insurance etc. In other words, we can say that the cost of earning revenue is an expense.

17. Expenditure

The amount which is paid for increasing profit earning capacity of business is called expenditure. It is of long period nature.

18. Income

That amount which increases the capital of the business is called income. The excess of revenue over expenses is also called income. (**Income= Revenue- Expenses**)

19. Loss

When expenses incurred are more than revenue then this excess of expenses is called loss. This reduces the capital of the business.

20. Gain

It is a monetary receipt as a result of business transaction. The excess of revenue over the expenses is called gain.

21. Cost

Total of direct or indirect expenses which are incurred for the production of goods and services is called cost. Like the cost of raw material cost of labor and cost of other services used to make the article is called its total cost.

22. Discount

Concession a rebate allowed by a businessman to its customer is called a discount. it may be of two types: –



a. Trade discount

When a trader allows a concession to its customers on the list price, it is known as trade discount. It is not recorded in the books. It is stated in the invoice.

b. Cash discount

When a trader allows a concession to the customer to make payment in cash or by cheque, it is known as cash discount. It is recorded in the books. When cash discount is allowed customer is required to pay the less due amount, so it encourages the customer to pay as early as possible.

23. Debtor

The person, firm or an organization who takes goods or services on credit from the business are called debtors of the business. In other words, the person, firm or an organization who owes money or Money's worth to the business is called debtor.

24. Creditors

The person, firm or an organization from whom goods or services are purchased on credit by the business are called creditors of the business. The business owes money to them. The amount payable to creditors is a liability of the business.

25. Bill Receivables

The total amount which is to be received in business is called receivables.

26. Bill Payables

The total amount which is to be paid by the business is called payables.

27. Entry

Recording of the transaction in account books is called making an entry or the record of a transaction in books is called an entry.

28. Turnover

The total amount of cash and credit sales during a particular period is called turnover.

29. Insolvent

A person is said to be insolvent when he or she is incapable to meet all his or her liabilities. Such a person has more liability than assets.

30. Solvent: A person or entity who is in a position to pay his/its debts.

31. Bad debts

The amount which could not be recovered from debtors due to his insolvency or disability to pay is called bad debts.

32. Vouchers

The written document through which financial transactions are recorded in the books is called voucher.

33 Account

A list of all transactions relating to a person, property, income expenses is called into account. It is a tabular statement containing all the transaction of same nature at one place under a common heading in a systematic manner.

34 Debit and credit

Every account has two sides. Left side is called the debit side and the right side is called the credit side. In short, it is Dr. and Cr.

35 Commission

In a business activity, a remuneration is paid to the agent for his services, is called commission

36. Balance Sheet: A statement of balances of assets and liabilities.

37. Book Value: Value of assets as existing in the books of accounts.

38. Books of Accounts: Books in which transactions are recorded or transferred (posted).

39. Financial Statements or Final Accounts: Statements prepared at the end of the accounting period to determine financial performance and financial position