MEANING OF KEY TERMS USED IN THE CHAPTER

1.	**Financial Statements**	Financial Statements are the statements which show the financial performance and financial position of the business. It includes Trading Account, Profit & Loss Account and Balance Sheet.
2.	**Trading Account**	Trading Account shows gross profit earned or gross loss incurred. It is credited with net sales, other direct incomes and closing stock. It is debited by opening stock, net purchases and direct expenses, *i.e.*, wages, freight, carriage inwards, etc.
3.	**Profit & Loss Account**	Profit & Loss Account shows net profit earned or net loss incurred. It is credited with gross profit and other incomes and debited with indirect expenses. The difference between the totals of two sides is either net profit or net loss.
4.	**Balance Sheet**	Balance Sheet shows the financial position of the business. It is a statement to which balances of assets, liabilities and capital accounts are showed at a particular date.
5.	**Capital Expenditure**	Capital Expenditure is that expenditure which gives benefit of enduring nature, *i.e.*, the benefit of which extends to a period or periods beyond the accounting period.
6.	**Revenue Expenditure**	Revenue Expenditure is that expenditure the benefit of which is exhausted within the accounting period.
7.	**Deferred Revenue Expenditure**	Deferred Revenue Expenditure is expense or loss incurred by the firm which are written off in more than one accounting period. They are categorised as Fictitious Assets.
8.	**Capital Receipts**	Capital Receipts are those receipts which are not received in the normal course of business, such as capital introduced, loan received, etc.
9.	**Revenue Receipts**	Revenue Receipts are those receipts which are received in the normal course of business, such as revenue from sale of goods and services.
10.	**Contingent Liability**	Contingent Liability is a liability that becomes payable on the happening of an event and not otherwise.
11.	**Grouping**	Grouping means placing items of one nature under a common head.
12.	**Marshalling**	Marshalling is arranging the assets and liabilities in a particular order, *i.e.*, in order of liquidity or in order of permanence.
13.	**Opening Entry**	Opening Entry is the Journal entry through which the closing balances of the previous year are brought forward in the current year's books of account.

CHAPTER SUMMARY

- **Financial Statements** are organised summaries of detailed information about the financial position and performance of an enterprise. The term Financial Statements is used to denote only two basic statements:
  - (*i*) **Trading and Profit & Loss Account (or Income Statement)** which shows the financial performance (*i.e.*, profit earned) of business operations during an accounting period.
  - (*ii*) **Balance Sheet (or Position Statement)** which shows the financial position of an enterprise at a particular date.

- **Objectives and Importance of Financial Statements:**
  - (*a*) **Trading and Profit & Loss Account:** (*i*) Ascertaining Gross Profit or Gross Loss; (*ii*) Ascertaining Net Profit or Net Loss; (*iii*) Comparison with Previous Year's Profit; (*iv*) Detail of Direct and Indirect Expenses; (*v*) Preparing Balance Sheet; (*vi*) Maintaining Provisions and Reserves; and (*vii*) Calculating accounting ratios.
  - (*b*) **Balance Sheet:** (*i*) Ascertaining financial position; (*ii*) Comparison with Previous Year; (*iii*) Analysis of Individual items; and (*iv*) Calculating accounting ratios.
- **Users of Financial Statements:** The information conveyed through Financial Statements is used by the management, investors, potential investors, lenders, short-term creditors, employees, customers, government and their agencies, tax authorities and stock exchanges to satisfy their different information needs.
- **Capital Expenditure** is the amount of expenditure incurred by an enterprise on purchase of fixed assets that are used in the business to earn income and are not intended for resale. The benefit of Capital Expenditure extends beyond the financial year.
- **Revenue Expenditure** is the amount of expenditure incurred on running of the business. The benefit of Revenue Expenditure expires within a financial year.
- **Deferred Revenue Expenditure** is a Revenue Expenditure, the benefit of which extends beyond an accounting period. *Example:* Unduly large expenditure on advertisement, say, to introduce a new product.
- **Final Accounts** include (*i*) Trading, Profit & Loss Account and (*ii*) Balance Sheet. Final Accounts are prepared on the basis of a Trial Balance.
- **Trading Account** is the account, which shows the gross profit or gross loss. Its contents are Revenue Receipts (such as sales, services rendered, etc.) on the credit side and Revenue Expenditure (such as cost of goods sold or services rendered) on the debit side.
- **Profit & Loss Account** is the account, which shows the net profit or net loss of the business for an accounting period. It is credited with the gross profit (or debited with gross loss) and non-business revenue income and debited with indirect revenue expenses.
- **Balance Sheet** is a statement, which sets out the assets and liabilities of a firm or an institution as at a certain date. It is true on that particular date as every transaction has an impact on the Balance Sheet.
- **Grouping:** It refers to putting items of similar nature under a common accounting head.
- **Marshalling:** It refers to arrangement of assets and liabilities in a particular order in the Balance Sheet. Assets and Liabilities are shown in the Balance Sheet either in order of **liquidity** or in order of **permanence**.
- **Contingent Liabilities** are the liabilities that may or may not take place. The liability becomes payable on happening of a certain event.
- **Presentation of Financial Statements:** The Trading and Profit & Loss Account and the Balance Sheet can be presented either in **Horizontal Form** or in **Vertical Form**.
- **Opening Entry:** Opening Entry is the Journal entry through which the closing balances of the previous year are brought forward in the current year's books of account.