

UNIT 3: ACCOUNTING PRINCIPLES

Level

REMEMBER
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1. What is accounting?
 - A. Recording financial transactions
 - B. Managing human resources
 - C. Conducting market research
 - D. Building physical assets

Answer: A. Recording financial transactions

2. What is the primary objective of accounting?
 - A. Maximizing profits
 - B. Providing financial information
 - C. Minimizing expenses
 - D. Employee satisfaction

Answer: B. Providing financial information

3. Which of the following is not an objective of accounting?
 - A. To facilitate decision-making
 - B. To maintain confidentiality
 - C. To provide information for taxation
 - D. To measure financial performance

Answer: B. To maintain confidentiality

4. The sequence of accounting procedures is collectively known as:
 - A. Accounting principles
 - B. Accounting cycle
 - C. Accounting standards
 - D. Accounting policies

Answer: B. Accounting cycle

5. : Which of the following is the correct order of the accounting cycle?
 - A. Adjusting entries, trial balance, financial statements
 - B. Financial statements, adjusting entries, trial balance
 - C. Trial balance, adjusting entries, financial statements
 - D. Trial balance, financial statements, adjusting entries

Answer: C. Trial balance, adjusting entries, financial statements

6. : What is the purpose of the trial balance?
 - A. To identify errors in the accounting records
 - B. To record adjusting entries
 - C. To prepare financial statements
 - D. To close the accounting cycle

Answer: A. To identify errors in the accounting records

7. Financial accounting primarily deals with:
 - A. Internal decision-making
 - B. External reporting to stakeholders
 - C. Cost analysis
 - D. Budgeting

Answer: B. External reporting to stakeholders

8. Cost accounting is concerned with:
- A. Recording financial transactions
 - B. Measuring and analyzing costs
 - C. Managing investments
 - D. Preparing financial statements

Answer: B. Measuring and analyzing costs

9. Management accounting is focused on:
- A. External financial reporting
 - B. Providing information for decision-making within the organization
 - C. Cost control
 - D. Auditing

Answer: B. Providing information for decision-making within the organization

10. GAAP stands for:
- A. Generally Accepted Accounting Procedures
 - B. Generally Acknowledged Accounting Principles
 - C. Generally Accepted Auditing Practices
 - D. Generally Accepted Accounting Principles

Answer: D. Generally Accepted Accounting Principles

11. The convention that assumes an entity will remain in business for the foreseeable future is:
- A. Materiality
 - B. Going Concern
 - C. Consistency
 - D. Conservatism

Answer: B. Going Concern

12. Which concept emphasizes recording transactions at their original cost?
- A. Money Measurement
 - B. Historical Cost
 - C. Dual Aspect
 - D. Matching

Answer: B. Historical Cost

13. If an item is not significant enough to influence the decision of a user, it is considered under the concept of:
- A. Materiality
 - B. Consistency
 - C. Prudence
 - D. Dual Aspect

Answer: A. Materiality

14. The principle that assumes the entity will not understate its assets or income is known as:
- A. Prudence
 - B. Consistency
 - C. Materiality
 - D. Going Concern

Answer: A. Prudence

15. : The concept that requires the use of estimates and judgment in preparing financial statements is:

- A. Materiality
- B. Prudence
- C. Substance Over Form
- D. Consistency

Answer: C. Substance Over Form

16. Which accounting concept states that accounting information should be prepared and presented for the users of financial statements to make informed decisions?

- A. Relevance
- B. Reliability
- C. Comparability
- D. Understandability

Answer: D. Understandability

17. The convention that assumes the business will continue operating indefinitely is:

- A. Consistency
- B. Materiality
- C. Going Concern
- D. Prudence

Answer: C. Going Concern

18. The concept that requires similar transactions to be treated in a consistent manner is:

- A. Materiality
- B. Consistency
- C. Dual Aspect
- D. Prudence

Answer: B. Consistency

19. The principle that states revenue and expenses should be recognized in the accounting period in which they are earned or incurred is:

- A. Matching
- B. Revenue Recognition
- C. Consistency
- D. Dual Aspect

Answer: A. Matching

20. Which accounting concept emphasizes the importance of recording both the debit and credit aspects of a transaction?

- A. Dual Aspect
- B. Consistency
- C. Prudence
- D. Going Concern

Answer: A. Dual Aspect

21. The convention that suggests a more conservative approach in recognizing profits and assets is:

- A. Prudence
- B. Consistency

- C. Materiality
- D. Going Concern

Answer: A. Prudence

22. The concept that assumes an entity will not overstate its assets or income is known as:

- A. Prudence
- B. Consistency
- C. Materiality
- D. Going Concern

Answer: D. Going Concern

23. Which principle requires that financial statements should be prepared with the assumption that the entity will remain in operation for the foreseeable future?

- A. Matching
- B. Going Concern
- C. Materiality
- D. Prudence

Answer: B. Going Concern

24. Which concept ensures that financial statements can be compared over different periods and between different entities?

- A. Materiality
- B. Comparability
- C. Consistency
- D. Prudence

Answer: B. Comparability

25. The convention that allows accountants to choose between multiple acceptable accounting methods is:

- A. Consistency
- B. Comparability
- C. Materiality
- D. Prudence

Answer: A. Consistency

UNDERSTA
ND

1. Meaning of Accounting:
- a) Recording financial transactions
 - b) Interpreting financial data
 - c) Both a and b
 - d) None of the above

Answer: c. Both a and b

2. Objectives of Accounting:
- a. Profit maximization
 - b. Decision-making
 - c. Wealth maximization
 - d. All of the above

Answer: d. All of the above

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MCQs

3. Accounting Cycle:
- a. A single step process
 - b. A continuous process
 - c. A series of steps in sequence
 - d. Random and unpredictable

Answer: c. A series of steps in sequence

4. Branches of Accounting - Financial Accounting:
- a. Focuses on internal decision-making
 - b. Emphasizes historical data
 - c. Aims at providing information to external users
 - d. Both a and b

Answer: c. Aims at providing information to external users

5. Branches of Accounting - Cost Accounting:
- a. Deals with the recording of financial transactions
 - b. Focuses on the cost of production
 - c. Aims at preparing financial statements
 - d. Both b and c

Answer: b. Focuses on the cost of production

6. Branches of Accounting - Management Accounting:
- a. Primarily concerned with reporting to external parties
 - b. Provides information for planning and decision-making
 - c. Focuses on compliance with regulations
 - d. Both a and c

Answer: b. Provides information for planning and decision-making

7. Concepts and Conventions of Accounting:
- a. Money Measurement Concept
 - b. Materiality Concept
 - c. Both a and b
 - d. Neither a nor b

Answer: c. Both a and b

8. GAAP stands for:
- a. Generally Accepted Accounting Principles
 - b. Generally Acknowledged Accounting Practices
 - c. Generally Applied Accounting Procedures
 - d. Generally Authorized Accounting Protocols

Answer: a. Generally Accepted Accounting Principles

9. The Going Concern Concept assumes:
- a. The business will continue to operate indefinitely
 - b. The business will cease to exist soon
 - c. The business will only operate for a fixed period
 - d. None of the above

Answer: a. The business will continue to operate indefinitely

10. Which accounting principle requires revenue to be recognized when it is earned and realizable?
- a. Matching Principle
 - b. Revenue Recognition Principle
 - c. Conservatism Principle
 - d. Materiality Principle

Answer: b. Revenue Recognition Principle

11. The primary purpose of a trial balance is to:
- a. Determine the financial position of a business
 - b. Identify errors in the accounting records
 - c. Prepare financial statements
 - d. Both b and c
- Answer: d. Both b and c

12. The formula for calculating Net Income is:
- a. Revenue - Expenses
 - b. Assets - Liabilities
 - c. Revenue + Expenses
 - d. Assets + Liabilities

Answer: a. Revenue - Expenses

13. Which financial statement shows the financial position of a business at a specific point in time?
- a. Income Statement
 - b. Balance Sheet
 - c. Statement of Cash Flows
 - d. Retained Earnings Statement

Answer: b. Balance Sheet

14. The cost of goods sold is subtracted from net sales to calculate:
- a. Gross profit
 - b. Operating profit
 - c. Net income
 - d. Net profit margin

Answer: a. Gross profit

15. In cost accounting, direct costs are:
- a. Costs that can be traced directly to a cost object
 - b. Costs that cannot be traced to a cost object
 - c. Indirect costs
 - d. Both b and c

Answer: a. Costs that can be traced directly to a cost object

16. The break-even point is the point at which:
- a. Total revenue equals total expenses
 - b. Total revenue exceeds total expenses
 - c. Total revenue is less than total expenses
 - d. Total fixed costs are covered by total variable costs

Answer: a. Total revenue equals total expenses

17. Which management accounting technique involves comparing actual performance to a budget?
- a. Variance analysis
 - b. Ratio analysis
 - c. Trend analysis
 - d. Cost-volume-profit analysis

Answer: a. Variance analysis

18. Return on Investment (ROI) is calculated as:
- a. Net Profit / Total Assets
 - b. Net Profit / Shareholder's Equity
 - c. Net Profit / Total Revenue
 - d. Net Profit / Investment Cost

Answer: a. Net Profit / Total Assets

19. The matching principle in accounting refers to:
- a. Matching expenses with revenue in the period earned
 - b. Matching liabilities with assets
 - c. Matching cash flows with expenses
 - d. Matching revenue with liabilities

Answer: a. Matching expenses with revenue in the period earned

20. The convention of conservatism suggests that:
- a. Assets and revenues should be overstated
 - b. Liabilities and expenses should be understated
 - c. Assets and revenues should be understated
 - d. Liabilities and expenses should be overstated

Answer: d. Liabilities and expenses should be overstated

21. Which accounting concept assumes that the business will continue operating for the foreseeable future?
- a. Money Measurement Concept
 - b. Going Concern Concept
 - c. Cost Concept
 - d. Dual Aspect Concept

Answer: b. Going Concern Concept

22. Which of the following is not an essential element of financial statements?
- a. Income statement
 - b. Cash flow statement
 - c. Statement of retained earnings

d. Trial balance

Answer: d. Trial balance

23. The principle of consistency in accounting states that:
- a. Similar events should be accounted for in a similar manner
 - b. Accounting methods should be changed frequently
 - c. Different events should be accounted for in a similar manner
 - d. Accounting methods should be changed based on management's preference

Answer: a. Similar events should be accounted for in a similar manner

24. Which of the following is an external user of financial statements?
- a. Manager
 - b. Shareholder
 - c. Employee
 - d. All of the above

Answer: b. Shareholder

25. The accrual basis of accounting recognizes revenue and expenses:
- a. When cash is received or paid
 - b. When earned or incurred, regardless of when cash is received or paid
 - c. Only when cash is received
 - d. Only when cash is paid

Answer: b. When earned or incurred, regardless of when cash is received or paid

APPLY

1. What is the primary purpose of accounting?
- a. Entertainment
 - b. Record-keeping
 - c. Decision-making
 - d. Socializing

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MCQs

Answer: c) Decision-making

2. What is the main objective of financial accounting?
- a. Predicting future trends
 - b. Providing information to external parties
 - c. Controlling internal operations
 - d. Budgeting for the upcoming year

Answer: b) Providing information to external parties

3. Which of the following is a branch of accounting that focuses on costs and expenses within a business?
- a) Financial accounting
 - b) Cost accounting
 - c) Management accounting
 - d) Tax accounting

Answer: b) Cost accounting

4. The process of systematically recording, classifying, and summarizing financial transactions is known as:
- a) Auditing
 - b) Budgeting
 - c) Accounting cycle
 - d) Financial reporting

Answer: c) Accounting cycle

5. Which branch of accounting is concerned with providing information to help management in decision-making?
- a) Cost accounting
 - b) Management accounting
 - c) Financial accounting
 - d) Tax accounting

Answer: b) Management accounting

6. Generally Accepted Accounting Principles (GAAP) are:
- a) Guidelines for conduct in the accounting profession
 - b) Rules that must be followed by all businesses
 - c) Standards that provide a common set of procedures
 - d) Suggestions for best practices in accounting

Answer: c) Standards that provide a common set of procedures

7. What is the purpose of accounting conventions?
- a) To make accounting more interesting
 - b) To simplify complex transactions
 - c) To provide a framework for financial reporting
 - d) To challenge traditional accounting practices

Answer: c) To provide a framework for financial reporting

8. Which of the following is a basic accounting concept that assumes a business will continue operating indefinitely?
- a) Conservatism
 - b) Going Concern
 - c) Consistency
 - d) Materiality

Answer: b) Going Concern

9. What is the key difference between financial accounting and management accounting?
- a) Financial accounting is focused on external reporting, while management accounting is focused on internal decision-making.
 - b) Financial accounting is only concerned with expenses, while management accounting is concerned with revenue.
 - c) Financial accounting is only relevant to small businesses, while management accounting is relevant to large corporations.
 - d) Financial accounting is focused on tax reporting, while management accounting is focused on regulatory compliance.

Answer: a) Financial accounting is focused on external reporting, while management accounting is focused on internal decision-making.

10. Which financial statement provides a snapshot of a company's financial position at a specific point in time?

- a) Income statement
- b) Statement of cash flows
- c) Balance sheet
- d) Retained earnings statement

Answer: c) Balance sheet

11. What does the term "debit" represent in accounting?

- a) An increase in assets or expenses
- b) A decrease in liabilities or income
- c) An increase in liabilities or income
- d) A decrease in assets or expenses

Answer: a) An increase in assets or expenses

12. What is the purpose of a trial balance in the accounting process?

- a) To prepare financial statements
- b) To ensure the equality of debits and credits
- c) To analyze business transactions
- d) To record adjusting entries

Answer: b) To ensure the equality of debits and credits

13. Which of the following is a current liability?

- a) Notes payable (due in 3 years)
- b) Accounts payable
- c) Long-term debt
- d) Common stock

Answer: b) Accounts payable

14. In cost accounting, direct costs are directly attributable to:

- a) Manufacturing a product
- b) Selling a product
- c) Administering the business
- d) Financing the business

Answer: a) Manufacturing a product

15. Which cost classification includes both direct materials and direct labor?

- a) Variable costs
- b) Prime costs
- c) Conversion costs
- d) Indirect costs

Answer: b) Prime costs

16. What is the purpose of a budget in management accounting?
- a) To track historical financial performance
 - b) To plan and control future operations
 - c) To report financial results to external parties
 - d) To comply with tax regulations

Answer: b) To plan and control future operations

17. Which accounting concept requires that expenses be recorded when they are incurred, not necessarily when the cash is paid?
- a) Matching principle
 - b) Revenue recognition principle
 - c) Time period principle
 - d) Materiality principle

Answer: a) Matching principle

18. The accrual basis of accounting recognizes revenue and expenses:
- a) When cash is received or paid
 - b) When they are incurred, regardless of when cash is exchanged
 - c) Only when cash is exchanged
 - d) Only when they are paid in cash

Answer: b) When they are incurred, regardless of when cash is exchanged

19. Which financial statement reports the company's revenues and expenses over a specific period of time?
- a) Balance sheet
 - b) Income statement
 - c) Statement of cash flows
 - d) Retained earnings statement

Answer: b) Income statement

20. What is the primary goal of cost accounting?
- a) To determine the selling price of a product
 - b) To control and reduce costs
 - c) To comply with tax regulations
 - d) To report financial results to external parties

Answer: b) To control and reduce costs

21. What is the purpose of the statement of cash flows?
- a) To report the company's financial position at a specific point in time
 - b) To show the change in equity during a period
 - c) To explain the difference between net income and cash provided by operating activities
 - d) To report the company's revenues and expenses

Answer: c) To explain the difference between net income and cash provided by operating activities

22. Which accounting principle requires that the financial statements of a business be prepared assuming that it will remain in operation indefinitely?

- a) Consistency
- b) Materiality
- c) Going Concern
- d) Conservatism

Answer: c) Going Concern

23. Which of the following is an example of a current asset?

- a) Land
- b) Buildings
- c) Accounts receivable
- d) Equipment

Answer: c) Accounts receivable

24. What is the purpose of the adjusting entries in the accounting cycle?

- a) To correct errors in the financial statements
- b) To record transactions that occurred after the end of the accounting period
- c) To ensure that the revenue recognition and matching principles are followed
- d) To prepare the financial statements for external reporting

Answer: c) To ensure that the revenue recognition and matching principles are followed

25. Which accounting principle requires that an asset should be recorded at the amount paid for it, regardless of its current market value?

- a) Historical cost principle
- b) Revenue recognition principle
- c) Matching principle
- d) Materiality principle

Answer: a) Historical cost principle

Analyze

1. Meaning and Objectives of Accounting:

Meaning: Accounting is the systematic recording, analysing, and reporting of financial transactions of a business.

Objectives: To provide accurate financial information, facilitate decision-making, and ensure accountability.

2. **Accounting Cycle:**

It's a series of steps in the accounting process, including journalizing transactions, posting to ledgers, preparing trial balances, adjusting entries, creating financial statements, and closing the books.

3. **Financial Accounting:** Focuses on external reporting for stakeholders and follows generally accepted accounting principles (GAAP).

4. **Cost Accounting:** Involves tracking and analyzing costs within a business to

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improve efficiency and reduce expenses.

5. **Management Accounting:** Provides internal information to help management make informed decisions.

6. **Financial Accounting:**

Involves the preparation of financial statements (income statement, balance sheet, cash flow statement) for external users like investors and creditors.

7. **Cost Accounting:**

Concentrates on the costs associated with producing goods or services, helping management control and reduce expenses.

8. **Management Accounting:**

Aids internal decision-making by providing information on costs, budgets, and performance metrics.

9. **Entity Concept:** Treats the business as a separate entity from its owners.

10. **Money Measurement Concept:** Only transactions that can be expressed in monetary terms are recorded.

11. **Consistency:** Requires a business to use the same accounting methods and procedures from one period to the next.

12. **Materiality:** Emphasizes the significance of an item's impact on financial statements.

13. **GAAP (Generally Accepted Accounting Principles):**

These are a set of standardized principles and guidelines used for financial reporting, ensuring consistency and comparability.

14. **Accrual Basis Accounting:**

Records revenues and expenses when they are earned or incurred, regardless of when the cash is received or paid.

15. **Cash Basis Accounting:**

Recognizes revenues and expenses only when actual cash transactions occur.

16. **Double-Entry Accounting:**

Every transaction has equal and opposite effects, with debits equaling credits to maintain the accounting equation.

17. **Trial Balance:**

A list of all general ledger accounts with their balances, used to ensure debits equal credits before preparing financial statements.

18. **Income Statement:**

Summarizes revenues and expenses to determine the net income or loss of a business over a specific period.

19. **Balance Sheet:**

Shows a company's financial position at a specific point in time, listing assets, liabilities, and equity.

20. **Cash Flow Statement:**

Presents the inflow and outflow of cash and cash equivalents over a specified period, categorized into operating, investing, and financing activities.

21. **Depreciation:**

The systematic allocation of the cost of a long-term asset over its useful life.

Evaluate

1. Objectives of Accounting:		
Objectives	Options	Answer
A. Maximize profits	i. To maximize financial performance	A - i
B. Provide financial information to users	ii. To facilitate decision-making	B - ii
C. Minimize expenses	iii. To ensure compliance with	C - v

	regulations	
D. Promote ethical behavior	iv. To enhance stakeholder trust	D - iv
E. Control management decisions	v. To optimize resource allocation	E - iii

2. Accounting Cycle:

Activities	Options	Answer
A. Budgeting	i. Planning and forecasting	A - i
B. Marketing	ii. Operational activities	B - v
C. Hiring employees	iii. End-of-period activities	C - iv
D. Receiving payment from customers	iv. Human resources management	D - ii
E. Closing the books	v. Revenue generation	E - iii

3. Branches of Accounting:

Branches of Accounting	Options	Answer
A. Cost Accounting	i. External reporting	A - iv
B. Management Accounting	ii. Decision support	B - ii
C. Tax Accounting	iii. Government compliance	C - iii
D. Financial Accounting	iv. Cost control	D - i
E. Social Accounting	v. Corporate social responsibility	E - v

EVALUATE

1. Financial accounting focuses on the internal management of a company's resources.
 - i. False
2. Cost accounting involves the identification and analysis of business costs.
 - i. True
3. Management accounting is primarily concerned with reporting financial information to external parties.

- i. False
- 4. The accounting cycle is a series of steps that begins with the recording of financial transactions and ends with the preparation of financial statements.

- i. True
- 5. One of the main objectives of accounting is to provide financial information for decision-making.
- a. True
- 6. GAAP stands for Generally Accepted Accounting Principles and represents a standardized set of rules and guidelines for financial accounting.

- a. True
- 7. Financial accounting is concerned with the future projections of a company's financial performance.

- a. False
- 8. Cost accounting is particularly useful for determining the profitability of individual products or services.

- a. True
- 9. Management accounting is primarily retrospective, focusing on historical financial data.

- a. False
- 10. The accounting equation is $\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$.

- a. True
- 11. Financial accounting is mainly used for internal decision-making within a company.

- a. False
- 12. Depreciation is an accounting concept that reflects the reduction in the value of an asset over time.

- a. True
- 13. GAAP is a global standard that is universally accepted and applied in the same way across all countries.

- a. False
- 14. The primary objective of cost accounting is to ensure compliance with tax regulations.

- a. False
- 15. Management accounting involves the preparation of financial statements for external stakeholders.

- a. False
- 16. In the accounting cycle, the trial balance is prepared after adjusting entries.

- a. True
- 17. GAAP allows for different accounting treatments for the same transaction, providing flexibility to companies.

a. False
18. Financial accounting is governed by strict legal regulations, and companies have limited flexibility in its application.

a. True
19. The revenue recognition principle states that revenue should be recognized when it is earned, regardless of when cash is received.

a. True
20. The primary purpose of accounting concepts and conventions is to create a standardized framework for financial reporting.

a. True

CREATE

1. Accounting is the process of recording, _____, and communicating financial information about an economic entity.

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in the
blanks

Answer: classifying

2. The primary objective of accounting is to provide information that is useful for _____ decision-making.

Answer: economic

3. _____ involves summarizing financial information in a structured way, typically in financial statements.

Answer: Reporting

4. One of the key objectives of accounting is to ensure the _____ of financial statements for users.

Answer: reliability

5. The _____ principle states that accounting information should be based on objective evidence.

Answer: objectivity

6. The accounting cycle starts with the analysis of _____ transactions.

Answer: business

7. _____ is the process of recording business transactions in the accounting system.

Answer: Journalizing

8. The trial balance is prepared to ensure that _____ and _____ are equal.

Answer: debits, credits

9. Adjusting entries are made to record revenues and expenses that have not been _____ in the regular journal entries.

Answer: captured

10. The last step in the accounting cycle is to prepare the _____ and _____ statements.

Answer: financial, closing

11. _____ accounting focuses on recording and summarizing financial transactions for individuals and businesses.

Answer: Financial

12. In _____ accounting, the emphasis is on providing information for internal management decision-making.

Answer: Management

13. _____ accounting involves the examination of financial records for legal or regulatory purposes.

Answer: Forensic

14. _____ accounting deals with the preparation and analysis of budgets to guide business operations.

Answer: Cost

15. _____ accounting involves the measurement and communication of environmental and social impacts.

Answer: Sustainability

16. The _____ concept assumes that a business will continue to operate indefinitely.

Answer: Going Concern

17. The _____ convention implies that accounting information should be presented conservatively.

Answer: Conservatism

18. The _____ concept states that accounting information should be relevant and reliable.

Answer: Relevance

19. The _____ concept requires that accounting records and statements be based on objective evidence.

Answer: Objectivity

20. The _____ convention suggests that accounting should follow established industry practices and standards.

Answer: Consistency