ACCOUNTING PRACTICES OF SOLE-PROPRIETORSHIP AND PARTNERSHIP ENTERPRISES:
A STUDY IN GUWAHATI CITY.

CHAPTER 1
INTRODUCTION

I. Introduction:

Accounting is the language of business. Business information is expressed by using accounting language. Information on various business activities, viz. financing, investing and operating activities; etc. are communicated through accounting medium to the users of this information. In the past, accounting was limited to book keeping only but now its scope has been widened to include other activities, such as tax accounting, cost accounting, management accounting, social accounting, green accounting etc. Accounting has also its influence on business planning and forecasting through analysis of financial statement.

Progress and prosperity of business depend upon the adoption of proper accounting practices. But most of the small business firms, engaged in trading activities, do not give proper attention towards accounting of their business transactions. They usually concentrate more on selling and buying activities of their products and are not serious on maintaining proper books

Nowadays, the needs of the customers have risen for which the business entities have to carry inventories of varieties of goods. Again, a substantial portion of the goods are sold generally on credit by sole proprietorships and partnership firms. It leads to an increase in the volume of investment in stocks and debtors.

As the business world is very competitive and the cost of running a business is going up, the business entities have to improve their financial performance by regular supervision and monitoring. Measurement of the results of business activities is done by preparing trial balance, trading account, profit and loss account, and balance sheet. They also keep records of sales, purchases, returns of sales and purchases, stocks, collections from trade debtors, and payments to trade creditors, etc. Again, these accounting information, are to be communicated to the tax authorities, banks or financial institutions, insurance companies, suppliers of goods, etc. The operation of business has become more complex over the years, accordingly accounting has also developed new concepts and techniques which are applied to meet the ever-increasing needs for financial information.

Accounting is a process which follows some prescribed rules and steps to record the daily business transactions in order to get the results.
thereof. As and when a transaction takes place in the business, the effect of that transaction is put to accounting process and recorded in the proper books of accounts. Record keeping in a business firm means to retain records of all necessary information in all aspects related to the business activities. Such business activities may be:

(i) Purchases of goods and services and consumables;
(ii) Sales of goods and services;
(iii) Payment received from the debtors;
(iv) Payment made to the suppliers;
(v) Purchase and sale of assets;
(vi) Taking of loans and settlement thereof,
(vii) Payment to the staff;
(viii) Transactions relating to capital and withdrawal thereof;
(ix) Payment for other activities related to the business, e.g., rent, hire charge, electricity and other operating expenses.

The above list is not exhaustive. There may be various types of items which require systematic recording in proper books of accounts. A systematic record keeping procedure also ensures proper preservation for evidential purposes, accurate and timely availability of all required data. It also facilitates control over the activities of the organisation by the proper authorities (owners, management etc).
It would not be out of reference to mention here that all business organisations are subject to the application of ‘Concept of Separate Entity’. So, each and every business firm invariably shall keep separate accounts for the business. In case of company form of organisations there is separation of ownership from the management, so the problem of keeping separate accounts for the company will not arise. But in case of sole proprietorship and partnership (unlimited) enterprises, there is no such separation of ownership from the management. These firms are very flexible types of business entity, and the owners has complete control over all the aspects of his business and can take direct and unrestricted managerial control in taking decisions concerning the management and the future of the business and act quickly and efficiently. Thus the sole proprietorship and partnership form of business organisations have derived the power to maintain necessary accounts of their business activities. But this does not mean that they can mix up their private (household) accounts with business accounts. The owners are obviously interested to know the result of the business periodically. Moreover, there are some legal bindings also which compels the owners to maintain proper accounts and to submit the same to the proper authorities. In this context section 9 of the Indian Partnership Act 1932 and section 55 of the Assam Value Added Tax Act, 2003 may be mentioned. Section 9 of the Partnership Act,1932, specifies that partners are bound to carry on the business of the firm to greatest common advantage, to be just
and faithful to each other, and to render true accounts and full information of all things affecting the firm to any partner, his heir or legal representative. Section 55 of AVAT Act, 2003 has spelt out under Rule 31 the names of books of accounts and other records to be maintained and has also outlined broad guidelines for the purpose of maintaining proper books of accounts and records for the dealers who are registered under this Act.

II. About Guwahati City:

It will be worthwhile to be acquainted with some important features of the study area before the researcher proceeds farther.

Guwahati is the head quarter of Kamrup (Metro) district. This district of was created bifurcating the old Kamrup district on 3rd February’2003. In the ancient period Guwahati was known as Pragjyotishpur. It is said that Guwahati derives its name from the Assamese words “Guwa” means areca nut and “Haat” means market. The city is located between 26°10'45" North Latitude and 91°45'0" North Longitude and situated the southern bank of the mighty river Brahmaputtra and the foothills of the Shillong Plateau.

The city is connected with Lokapriya Gopinath International Bardoloi Airport at Borjhar the distance to which is only 20 km from the heart of the city. It is well connected with railways and road services. The city is administered by the Guwahati Municipal Corporation having an administrative area of 216 km². It is the largest city of the entire North-East
states and is considered as the gateway to the northeast. According to Office of the Registrar General and Census Commissioner of India, the population of the city as on 01-03-2011 is 9,57,352 which has shown an increase of almost 64% over the population of the year 1991.

Guwahati city is now the largest cosmopolitan and commercial and educational hub of Assam and the north-eastern region of India. The commercial scenario of the city can be categorized by the growth of various commercial activities. The Tea Auction centre in the city play an important role in the international commerce. Besides, there are many important commercial places in the city like Ganeshguri, entire G.S. Road, Panbazar, Fancy Bazar, Athgaon, Adabari, Maligaon, Bhangagarh, Chandmari, Narengi, Basistha, Beltola, Rehabari, Palton Bazar etc. Important commercial establishment of the city can be categorized into wholesale, wholesale cum retail, retail only and retail service shops.

Unorganised sector has a dominant position in Guwahati retail market. Most of the trading activities are carried out by the small and medium sized retailers. Grocery stores, pharmacy, stationery stores, garment stores, hardware stores etc. falls under this large unorganised retail sector of Guwahati. Customers’ inclination to these retail stores is due to low-cost products, convenient location, friendly relationship with the retailers and most importantly to avail credit facility.
However, organised retail stores have entered into the market providing everything under one roof, with better facilities like parking, discounts, air-conditioned shopping etc. For example- Big Bazar, Pantaloon, Vishal megamart, Reliance trendz, etc have entered the market with a strong customer base.

Even though these big retailers have entered the Guwahati retail market but their position is still not as strong as those of small retailers because of their presence at the very next door. The official data on the contribution of small retailers in the economic growth of the state is not available. But the role of these establishments in the daily economic life of all classes of people can be well felt when a bandh is called by some organisations. These business enterprises are providing employment as well as a means of livelihood for many individuals.

Present study covers sole proprietorship and partnership enterprises that are doing business as traders, (i.e., as retailers and wholesalers) in Guwahati city.

III. STATEMENT OF THE PROBLEM:

A business enterprise, no matter how small, needs an effective accounting system to sustain and establish its long term operational and financial goals. With a good accounting system in operation the enterprise can manage the cash inflows and outflows, can forecast revenues and pay
bills, can measure the values of the assets and the worth of the business and can generate reports to have access to the capital/debt market. With the globalization of business, the size of business firm is also growing along with increase in the volume of business transactions. These require higher amount of investment in the form of equity and debt capital. There are many opportunities with new problems before the business firm. They have to take decisions with certain degree of precision to reap the benefit of the opportunities and to overcome the problems. Accounting plays an important role to formulate proper policies and to take informed decision.

Though most of the small business enterprises do not prepare financial reports showing the value of assets and liabilities for external users, banks and other financial institutions require these statements in various degrees while considering the loan applications. For this, banks and other financial institutions seek information in black and white on the volume of business handled, the system and procedure of accounting and financial statements of the business enterprise.

Generally Accepted Accounting Principles (GAAP) are the common set of accounting principles, standards and procedures that a business firm, especially companies, use to prepare and present their financial statements. Business firms like sole proprietorship firms and partnership firms may also apply these in the accounting process and in reporting their financial information to the appropriate authority, viz.,
Commissioner of Sales Tax in compliance with the legal formalities as outlined under section 55 of the Assam Value Added Tax. Application of accounting principles in recording business transactions and in preparing accounts and statements by the sample firms under study is examined during the course of the study.

The importance of accounting on the one hand, and trading or manufacturing or marketing activities on the other, is not comparable. Accounting is considered as a supporting activity for the success of a business entity. In the modern technology based economy and competitive business world, quick and reliable availability of information is a pre-condition for success of business and this information may be obtained from accounting. Accounting practices play a vital role in ascertaining overall results of the business.

The accounting practices of sole proprietorship and partnership firms is restricted to maintenance of cash book, ledger, and preparation of trial balance, trading account, profit and loss account and balance sheet and submitting these to various agencies such as tax authorities for verification of tax liability and to banks or financial institutions for seeking credit facilities. Further, a very few of such business entities use accounting to evaluate their financial performance and for decision making.
IV. REVIEW OF LITERATURE:

The study covers sole-proprietorship (sole proprietorship concerns) and partnership firms (unlimited) which are the regular registered dealers under VAT in Guwahati city. There is considerable research on the accounting practice adopted by corporate sector, but there is very little research on the accounting practices of small business firms.

Mahesh Kumar R Prajapati has conducted a study on ‘Accounting practices of wholesale and retail business organisation in Gujarat’ (www.shodhganga.inflibnet.ac.in). In his Ph. D. thesis submitted in Sardar Patel University, Gujrat, he found that the accounting in wholesale and retail business is restricted to cash book, ledger, trial balance, trading account, profit and loss account and balance sheet and submitting these to tax authorities and banks at the end of financial year for verification and tax purpose and for continuation of banking facilities. Further, very few businessmen use accounting for decision making and to evaluate their financial performance. He has mentioned that selling and buying are not the only main function of business but accounting is also an important function of business that plays and vital role in improving the financial position of the firms. Therefore, regular recording and accounting of business transactions are very essential to take immediate corrective decisions to solve the problems of business. He has suggested computerization of accounts since it is essential to enhance its quality and to speed up customer service. The
computerization of account enables businessmen to get all the required information at anytime without much cost. Thus, it reduces the cost of transactions and increases the financial position of businessmen.

A.S. Shiralashetti and S.S. Hugar ‘Accounting Practices in Business: A study of Wholesale and Retailers in Bijapur District, published in the Accounting World, ICFAI, December, 2007. They have found that progress and prosperity of business depend upon adoption of proper accounting practices. For a business to survive in the competitive era, accounting contributes significantly, irrespective of the period it relates to. But most businessmen give less attention towards accounting of their business transactions. They usually concentrate more on selling and buying of their products and this has been more in the case of wholesale and retail businesses. They also mentioned that it is very difficult for individuals or group of individuals to keep track of each and every event and transaction of the businesses during a particular period.

The studies above does not cover in detail the nature of accounting records maintained by the business entities and also have not mentioned anything on the application of GAAP in these accounts of Wholesale and Retailers.

Another study conducted by Sujay Khadilkar on ‘Retail Trade with special reference to Grocery Trade in Kolhapur city’(Ph. D. Thesis submitted to Symbiosis International University) has not focused on
accounts maintained by the retailers. He has simply observed that computerization of grocery retail trading is upcoming innovation in the accounting and identification systems of hypermarkets.

The on-going research study makes an effort to fill up this gap focusing primarily on the system of maintaining books of accounts, basis of accounting – accrual or cash, level of sophistication, adoption of GAAP and revenue recognition and the problems faced by the Sole-Proprietorship and Partnership Enterprises in accounting related matter.

V. OBJECTIVES OF THE STUDY:
The objectives of the research enquiry are as follows:

1. To examine the accounting procedure adopted by the Sole proprietorship and Partnership Enterprises

2. To examine application of GAAP and revenue recognition process applied by the Sole proprietorship and Partnership Enterprises.

3. To study financial reporting system of Sole proprietorship and Partnership Enterprises to access in the institutional credit.

4. To examine the compliance requirements and there adherence to the various legislative and other legal provisions.

5. To examine the problems faced by Sole proprietorship and Partnership Enterprises in maintenance of Accounts and preparation of financial statements.
VI. METHODOLOGY:

In order to meet the aforesaid objectives of the research study the researcher has adopted the following methodology.

(i) Universe of the Study and Selection of units of study (Sample):

The sole proprietorship and partnership enterprises that are doing business as traders, (i.e., as retailers and wholesalers) in Guwahati city is the universe of the study.

(ii) Sampling Design:

There are 15,239 regular registered dealers under Value Added Tax (VAT) in Guwahati city as on 31.03.2010. As per the record of the office of the Commissioner of Taxes, Assam, Guwahati. Of these 10,612 are sole proprietorship dealers; 2,641 are partnership dealers (all are unlimited firms); 1,941 are corporate sector dealers and 45 are Hindu Undivided Families. The sample is selected randomly from 10,612 Sole-proprietorship and 2,641 Partnership Enterprises. Thus, the population size N = 13,253.

Depending upon the time, accessibility and resource, a sample of 200 Sole-proprietorship and Partnership Enterprises have been selected at random from the population of 13,253 Sole-proprietorship and Partnership Enterprises for the present research study. The samples have been taken on proportionate basis which are as under:
Table 1.1: Population and Distribution of samples

<table>
<thead>
<tr>
<th>Type of firm</th>
<th>Population</th>
<th></th>
<th>Sample</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No</td>
<td>% of the total</td>
<td>No</td>
<td>% of the total</td>
</tr>
<tr>
<td>Sole-Proprietorship</td>
<td>10612</td>
<td>80</td>
<td>160</td>
<td>80</td>
</tr>
<tr>
<td>Partnership</td>
<td>2641</td>
<td>20</td>
<td>40</td>
<td>20</td>
</tr>
<tr>
<td>Total</td>
<td>13253</td>
<td>100</td>
<td>200</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Office of the Commissioner of Taxes, Assam (as on 31<sup>st</sup> March, 2010)

In course of the analysis of data, the sample enterprises are further classified into retailers and wholesalers. Collected data shows that out of 160 sole proprietors, there are 60 wholesalers (37.5%) and 100 (62.5%) retailers. Again it is found that no retail business is conducted by the sample partnership enterprises and all 40 such partnership firms are wholesalers. The final distribution of the sample enterprises is shown below.
Table 1.2: Distribution of sample business enterprises according to Ownership structure and Type of Trade

<table>
<thead>
<tr>
<th>Types of trade</th>
<th>Ownership Structure</th>
<th>Sole-proprietorship</th>
<th>Partnership</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retailers</td>
<td>100 (62.5%)</td>
<td>Nil</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Wholesalers</td>
<td>60 (37.5%)</td>
<td>40(100%)</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>160 (100%)</td>
<td>40(100%)</td>
<td>200</td>
<td></td>
</tr>
</tbody>
</table>

(iii) Sources of Data:

The study is mainly based on primary data. The primary data are collected through field survey with the help of schedules of questions and personal interviews with the proprietors and employees (accountants/bookkeepers) of the firms and practicing chartered accountants. Moreover, the debt providers and tax consultants are also interviewed with schedules of questions to take their perception on the accounting practices followed by the Sole-proprietorship and Partnership Enterprises. The secondary data are collected from various newspapers, journals, like the Accounting World, Business Line, the Hindu, Economic Times, Indian Express etc, various websites and related books.
VII. RESEARCH QUESTIONS:

During the course of the study effort has been made to get answer to the following key research questions.

(i) What procedure is adopted by the sample firms in maintaining the accounts?

(ii) Whether the sample firms apply GAAP in the recording accounts and in the presentation financial statements?

(iii) Whether the sample firms comply with the legal provisions that are applicable to these firms?

(iv) What are the problems faced by the sample firms in maintenance of Accounts and preparation of financial statements?

VIII. CHAPTER PLAN:

The chapter plan of the research study is as follows:

Chapter 1 : Introduction

Chapter 2 : Conceptual Framework

Chapter 3 : Books of Accounts Maintained By the Sample Business Enterprises

Chapter 4 : Application 0f Generally Accepted Accounting Principles (GAAP)

Chapter 5 : Problems in Accounting Practices

Chapter 6 : Findings and Recommendations
IX. LIMITATIONS OF THE STUDY:

The present study suffers from two important limitations. These are as below

1. The most important limitation of the study is the non-availability of related literature on the topic. The researcher has found only a few studies on the related topic which are reviewed and presented in the review of literature section.

2. Since the sample units are not under any compulsion to publish the annual report, data collected from the interview and schedule of questions are the main source of information for the study.

3. The study is confined to the Sole-proprietorship and Partnership Enterprises of Guwahati city. During the study it is found that local and community traditions have had some impact on the disclosure of information including accounting information of these enterprises where very limited legal binding is applicable. Therefore some of the respondents are reluctant to give some information required for the study. This information is collected by putting indirect questions to their employees, and in some cases the sample unit is replaced by a new sample unit of the same class.