CHAPTER 2
CONCEPTUAL FRAMEWORK

It is worthwhile to detail out the key concepts used in any research study. Present study is also developed with the application of certain concepts, a brief description of which is forwarded in the following paragraphs.

I. BUSINESS:

Literally speaking, the term ‘Business’ means to be busy. In the context of trade and commerce business includes all occupations in which people are busy in earning income either by production or purchase and sale of goods and services to satisfy the needs of other people. Keith and Gulbelline in their book ‘Introduction to Business Enterprise’ define business as a system to satisfy society’s needs and desires. According to Richard Norman Owens, “an enterprise engaged in production and distribution of goods for sale in a market or the rendering of services for a price”.

The Harvard Business School forwarded a definition of business in its golden jubilee conference in 1958 in the following sentence: “Business creates and delivers value satisfactions at a profit”. According to this definition, business means creation and distribution of various utilities such
as possession utility, form utility, time utility and place utility for consumer’s satisfaction at a certain price to earn profit.

According to Section 2(13) of the Income-tax Act, the term ‘Business’ means any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture. In simple language, business means any economic activity carried on with the objective of making profits.

According to Section 2 (7) of the Assam VAT Act, 2003 “Business” includes:

(a) any trade, commerce or manufacture;

(b) any adventure or concern in the nature of trade, commerce or manufacture;

(c) any transaction in connection with, or incidental to or ancillary to, trade, commerce, manufacture, adventure or concern;

(d) any transfer of property in goods involved in execution of a works contract or transfer of the right to use any goods for any purpose or delivery of goods on hire purchase or by any system of payment by instalments;

(e) any occasional transaction in the nature of such trade, commerce, manufacture, adventure or concern whether or not there is volume, frequency, continuity or regularity of such transaction.
According to this section it is not necessary that such trade, commerce, manufacture, adventure, concern or transaction is effected with a motive to make gain or profit. It is also not necessary that gain or profit should accrue from such trade, commerce, manufacture, adventure, concern or transaction.

In the present study the researcher uses the meaning of business as a synonym of trade and covers only wholesale trade and retail trade.

When goods are purchased in bulk from the producers for resale to retailers, it is known as wholesale trade. On the other hand, when goods are purchased in comparatively smaller quantities either from the wholesalers or producers to sell to the ultimate consumers, it is termed as retail trade. To operate these trades formally, an investor can choose any one or more of the following forms of business organisations: firm, Partnership firm, Private Limited Company, Public Limited Company, Co-operatives, Franchises etc.

The present research is conducted over sole proprietorship firms and partnership firms who are carrying on their business as retailers and wholesalers.

II. SOLE PROPRIETORSHIP AND PARTNERSHIP ENTERPRISES:

MEANING AND DEFINITION:

Sole Proprietorship and Partnership enterprises fall under informal and unorganised sector. In this context the National Commission for
Enterprises in the Unorganized Sector (NCEUS) has forwarded the following definition of informal sector. ‘It is the unorganized sector that consists of all unincorporated private enterprises owned by individuals or households engaged in the sale and production of goods and services operated on a proprietary or partnership basis and with less than ten total workers”.


Again Informal Sector refers to economic activities i.e., production and distribution of goods and services by the operating units of the households which essentially differ from the formal sector in terms of technology, economies of scale, use of labour intensive processes, and virtual absence of well maintained accounts.(Informal Sector in the Indian System of National Accounts, Rajiv Sharma and Sunita Chitkara; Expert Group on Informal Sector Statistics; Ministry of Statistics and Programme Implementation, New Delhi)

www.mospi.nic.in/GDP%2006.doc

In many Asian countries such as India, Indonesia, Philippines for the purpose of data collection, the unorganised segment of an economic activity (sector) is defined to comprise those operating units whose activity is not regulated under any legal provisions and/or which do not maintain any
regular accounts. This definition helps to demarcate the formal from the informal. As a matter of fact some countries have quite often used the terms ‘unorganised’ and ‘informal’ interchangeably.

For the purpose of present study, a business entity which is owned and managed by one individual is known as business. It is a form of business in which one person owns all the assets of the business, in contrast to a partnership or a company or a cooperative.

A sole proprietorship firm, does not pay separate income tax on the business, but reports all losses and profits on his/her individual tax return.

A partnership firm is not a separate legal entity. To establish a firm no legal formalities are necessary other than appropriate licensing to conduct business and registration under appropriate State Act.

Partnership is an association of two or more persons who agree to carry on a lawful business with the object of sharing profits and losses. The partners provide the capital and share the responsibility for running the business on an agreed basis. **Section 4 of Indian Partnership Act, 1932** defines a Partnership as “the relationship between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.”

**Essential Elements of Partnership:**

The definition of partnership as given in the Partnership Act, 1932 brings forth the following three distinct elements:
(a) There must be an association of two or more persons;

(b) There must be an agreement between all the persons concerned;

(c) The object of the agreement must be to share the profits of a business;

and

(d) The business must be carried on by all or any of them acting for all.

It should be noted that all the above essential elements must be present to form a partnership.

Present study is based on Sole-proprietorship and Partnership Enterprises of Guwahati City who are regular registered dealers under the Assam Value Added Tax Act, 2003 (AVAT Act, 2003). The act does not define a sole-proprietorship or a partnership but uses the term “Dealer” to include all such business organisations. Section 2(15) of the Act defines the term "dealer" as any person, who carries on (whether regularly or otherwise) the business of buying, selling, supplying or distributing goods directly or indirectly, for cash or deferred payment or for commission, remuneration or other valuable consideration,

In the above definition sole proprietorship and partnership enterprises are automatically covered under the term “Dealer”. So in the present study the term “dealer” is used on the basis of the above definition of the AVAT Act, 2003.
III. RETAIL TRADE AND WHOLESALE TRADE:

(a) Retail trade:

Retail trade is defined in the International Standard Industrial Classification (ISIC) as the re-sale (sale without transformation) of new and used goods to the general public, for personal or household consumption or utilisation (OECD Glossary of Statistical Terms). In retail business goods are directly sold to ultimate consumers in small quantity. The position of retailers in the hierarchy of distribution channel stands at the bottom. They are in direct contact with those buyers who purchase goods or services for ultimate use or consumption. Retailers purchase goods from wholesaler in small lots or quantities and sell the same to consumers as required. The retailers are the connecting link between wholesalers and consumers and render valuable services to both. Generally the retail firms are situated nearby the locality of the consumers. It procures different goods from different sources and makes it available to members of the society residing in its locality. These traders inform the producers through wholesalers about the attitudes, likes and dislikes, preferences, traditions and habits of consumers. The retail traders also play the role of adviser to the consumers and inform the consumers about the utility and other feature of the new products.
The High Court of Delhi defines the term ‘Retail’ in 2004, as a sale for final consumption in contrast to a sale for further sale or processing (i.e. wholesale), a sale to the ultimate consumer.

(b) Wholesale trade:

According to the OECD Glossary of Statistical Terms (Organization for Economic Co-operation and Development), ‘Wholesale trade is a form of trade in which goods are purchased and stored in large quantities and sold, in batches of a designated quantity, to resellers, professional users or groups, but not to final consumers’. Wholesalers, (sometimes also known as distributors), is an intermediate stage between the origin of a goods or services and its ultimate distribution to an end user through retail trade channels. Such trade involves buying goods in large quantity from producers and sells them in small quantities to retailers. The wholesalers take the responsibility of procuring and storing large quantities of goods for supply to the retailers as and when required by them. As such, wholesaler acts as an important link between the manufacturer and the consumers through retailers. The wholesalers provide information to the producers regarding the choice, interest and taste of the consumers received from the retailers so that the producers can produce the products as per the requirements of consumers.
The wholesalers purchase goods at retailer price with a percentage of
discount or commission on it. Retailer price means the price at which it will
be sold to the retailers. The discount allowed by the producers on retailer
price is the income of the wholesaler. The difference between retailer price
and maximum retail price (M.R.P.) is the income for the retailers. They
render valuable services to the society and have become indispensable in the
field of marketing.

IV. ACCOUNTING:

A business entity performs number of activities. These activities
may be classified as primary or main activities and auxiliary or
supplementary activities. The main activities may be in the form of
manufacture, sale and purchases of goods or rendering services. The
auxiliary activities are recording of transactions, receiving and payment of
cash, submission of tax returns and statutory compliance etc.

The ultimate motive of carrying on such activities is to earn profit.
The existence and continuation of a business depends on its ability to earn
profit. Every business is, therefore, interested to find out the amount of
profit earned (or loss incurred) during a particular period. For the purpose of
ascertaining the amount of profit earned (or loss incurred), a complete and
systematic record of business transactions are required to be maintained.
Accounting is a man made activity which has evolved over a period of time. It is a systematic exercise carried on for the purpose of recording, summarising and interpreting the results for the users of the information. Accounting helps a business in having a complete and systematic record of its business transactions, reporting the results of its operation and interpreting such results for the purpose of effective control of future operations or activities.

Earlier, all transactions were recorded in the books of account manually i.e. the accounting records are hand written. But, now-a-days, accounts are maintained in the computer by the big and medium size entities. In the computerised accounting system, the accounts are not written by the book-keepers in the books of account but are entered in the data base programme of the computer through key board.

Accounting for a business firm is a compulsion as well as it is desirable also. This may be understood from the following factors.

(i) To replace memory

(ii) To comply with legal requirements

(iii) To ascertain the results of operation of business regularly

(iv) To ascertain the financial position of the business regularly

(v) To control over assets and settlement of liabilities of the business

(vi) To raise loans, to control over investment in stocks and credit

(vii) To act as a legal evidence in case of any disputes,
(viii) To control over business expenditure,
(ix) To take decision by various users group
(x) To ascertain tax liability for insurance coverage,
(xi) To ascertain the value of the business in case of transfer of business or amalgamation etc.

Present study covers accounting practice by the sole proprietorship and partnership businesses in Guwahati city. The term ‘accounting practice’ is used to mean the exercise made by the sample units to record all financial transactions in the books, registers, khatas etc. as per their requirement, custom and necessity. Requirement and necessity to keep accounts may arise on account of measurement of periodic profit, tax liability and need of finance from financial institutions.

V. GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP)

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. GAAP is the commonly accepted ways of recording and reporting accounting information.
Accounting is a practical activity. Earlier, the accounting professionals were not very much concerned about the theoretical base of their profession. But gradually their job has been regarded as supplier of financial information for the use by the economic decision makers. With the growth in business and financial activities, this job of an accountant is being put under scrutiny. They have to satisfy all the users by their primary function as the preparer of financial statements. They have to apply certain concepts, conventions and postulates of accounting while preparing and presenting accounting information for the assistance of decision makers. Accounting professionals are generally required to discharge their duties relating to the following areas:

(a) which economic resources and obligations should be recorded as assets and liabilities in financial accounting,
(b) which changes in assets and liabilities should be recorded,
(c) when these changes should be recorded,
(d) how the assets and liabilities and changes in them should be measured,
(e) what information should be disclosed;
(f) how it should be disclosed; and
(g) which financial statement should be prepared.
The rules and principles applied in making decisions in the above areas and in translating such decision into practice through recording and preparing financial statements may be referred to as Generally Accepted Accounting Principles (GAAP).

Based on the recent development in the theory base of accounting, the traditional structure of GAAP has been restructured. These are now classified into the following four broad heads:

(a) Basic or Underlying Assumptions; (b) Principles; (c) Modifying Principles; and (d) Accounting Standards.

(a) **Basic or Underlying Assumptions:** Assumptions are traditions and customs developed over a period of time and well accepted by the accounting profession. Basic accounting assumptions provide a foundation for recording the transactions and preparing the financial statements there from. The following five assumptions are considered as basic assumptions of accounting. These are:

1. Accounting Entity
2. Accrual,
3. Going concern,
4. Money Measurement; and
5. Accounting Period.

(b) **Principles:** Basic accounting principles are the general decision rules which govern the development of accounting techniques. These principles
do not violate or conflict with the basic accounting assumptions. They work as complimentary to basic assumptions. Following are the basic accounting principles:

1. Dual Aspect.
2. Revenue recognition
3. Cost,
4. Matching,
5. Full Disclosure; and
6. Objectivity,

(c) **Modifying Principles:** Generally, the financial statements are prepared keeping in view the basic principles and assumptions of accounting. However, difficulties are faced in the application of accounting principles in certain situations which call for the modified application of the principles and assumptions of accounting. These constraints are referred to as *modifying principles* which are given below:

1. Materiality,
2. Conservatism (Prudence),
3. Cost-Benefit,
4. Timeliness,
5. Consistency,
6. Substance over Legal form; and
Application of the above accounting principles in recording business transactions and in preparing accounts and statements by the sample firms is examined during the course of the study.

(e) **Accounting Standards**: Accounting Standards are the established and accepted models which aim at providing excellent, adequate and unbiased treatment of accounting transaction/information and reporting the same in the financial statements to facilitate their users in forming rational and judicious decision. These are pronounced by the recognized professional bodies like, the Institute of Chartered Accountants of India. These accounting standards are to be complied with by the company form of business organisations. It is not mandatory on the part of Sole-proprietorship and Partnership Enterprises to comply with the requirement of accounting standards. But some of the standards, viz., Disclosure of Accounting policies (AS 1), Valuation of inventories (AS 2), Depreciation Accounting (AS 6), Revenue Recognition (AS 9), Accounting for Fixed Assets (AS 10), etc are useful for these organisations also. Complete or modified compliance of these accounting standards by Sole-proprietorship and Partnership Enterprises would certainly add value to their financial statements.
VI. BOOKS OF ACCOUNTS:

Books of accounts in relation to a business firm means the books in which the business transactions are recorded. These include journals, ledgers, cash books and other classified records. These books of accounts of a business firm represent the financial memory of the company, and are important document for performance measurement, continuity, decision-making, and control functions. Business firms are required to maintain proper books of accounts under various legislations, like Income tax, Companies Act, State VAT Acts etc.

Proper books of account are such books as will enable another merchant, a creditor of the insolvent for instance, to see the financial status of his debtors. The books of account of a merchant or trader kept in such a manner, that any competent person, by an examination of them, could ascertain and determine the real condition of his affairs; and if they be so kept, though imperfect, inartistic, and inaccurate in unimportant particulars, they will be treated as proper books of account. [Siegel v. His Creditors, 95 Cal. 409, 414 (Cal. 1892)]. [http://definitions.uslegal.com/p/proper-books-of-account]

The Value Added Tax Act, 2003 of the Government of Assam has outlined the requirement of maintenance of accounts and records by the dealers who are registered under this act. Section 55 of this Act has not spelt out specifically the names of books of accounts to be maintained but has
outlined broad guidelines for the purpose of maintaining proper books of accounts. It is laid down in section 55 (1) that every registered dealer or every dealer liable to pay tax under this Act shall keep a true and up-to-date account of the value of goods purchased or manufactured and sold by him or goods held by him in stock, in respect of each class of goods taxable at different rate of tax under this Act including input tax paid and output tax payable and, in addition to the books of account that a dealer maintains and keeps for the purpose referred to in this sub-section, he shall maintain and keep such registers and accounts in such form and in the manner as may be prescribed. Subsection (2) of section 55 says that every registered dealer or the dealer shall keep at his place of business all accounts, registers and documents maintained in the course of business and shall not remove elsewhere such accounts, registers and documents except in accordance with the requirement of law or except for any purpose for which just cause is shown to the satisfaction of the Commissioner.

Sub section (4) of Section 55 also states that if the Commissioner is of the opinion that the accounts kept and maintained by any dealer or class of dealers are not sufficiently intelligible and clear to enable him to verify the returns or to make any assessment under this Act, he may by an order, require such dealer or class of dealers, to keep such accounts, in such form and in such manner as he may, subject to rules made under this Act, direct. On the other hand according to Sub section (5) if the Commissioner is
satisfied that any dealer is not in a position to maintain accounts in accordance with the provisions of sub-section (1), he may, for reasons to be recorded in writing, exempt such dealer from the operation of the provisions of the said sub-section.

Assam Value Added Tax Act 2003 under Rule 31 in Chapter VI states the following specific rules for Maintenance of accounts and records’.

(1) Every dealer shall keep separate account of sales and purchases made:-
   (i) in the State, (ii) in the course of inter-state trade or commerce, (iii) in the course of import into India and (iv) in the course of export out of India.

(2) Every dealer registered under the Act shall maintain separate accounts for exempted goods.

(3) Every dealer shall keep separate purchase and sales accounts for different goods liable to tax at different rates of tax.

(4) Every dealer shall maintain separately a true and correct account of input tax relating to his purchases and of output tax relating to his sales against tax invoices in such a manner that the totaling made at the end of each tax period reflects the purchases and sales made under each tax rate and tax paid on such purchases and charged on such sales. Such purchase book or account shall record the date, invoice number, name of supplier, tax payer identification number (TIN) of domestic supplier, value of purchases and tax credit. The sales book shall have the provision for recording of sales to
registered and unregistered (final consumers) persons, separately, date and number of sales invoice and if the buyer is a registered taxpayer, his name, taxpayer identification number (TIN) and sale value and tax charged.

Specimen of sale and purchase registers is available in Form-44 and Form-45 respectively. These specimens are provided to facilitate a dealer for proper maintenance of accounts. A dealer may maintain account books as per his requirement and nature of business but these shall contain the information as per the specimen.

(5) Details of input tax calculations where the dealer is making both taxable and tax free sales.

(6) Original tax invoices for purchases on which tax has been charged, and invoices for purchases made without charge of Value Added Tax shall all be retained in date order.

(7) Copies of tax invoices related to taxable sales and invoices related to exempt sales shall all be retained in date and numerical order.

(8) Credit and debit notes issued and received shall all be retained in date and numerical order.

(9) Bank records, including statements, cheque book counter foils and pay-in-slips.
(10) Every dealer liable to pay tax under the Act, shall maintain, a Value Added Tax (VAT) account showing month wise details of total output tax, total input tax, total purchase tax, Central Sales Tax, reverse tax, net tax payable, tax paid and the input tax credit due for refund or carry forward to the subsequent return period, if any.

From the above discussion it is clear that all types of business firms have to maintain books and accounts as per their requirement considering the nature of business. Moreover, legal requirements also have a role in selecting which books of accounts are to be maintained. Sole proprietors and partnership firms have to furnish some vital accounting and other information to the State VAT authorities. So the kind of accounts books to be maintained by these business enterprises largely depends on the requirement under the rules of Assam Value Added Tax Act, 2003