ENTRI

Financial Accounting

Topic 1: **Accounting principles and accounting standards**

Accounting

According to AICPA (American Institute of Certified Public Accountants) it is defined as "the art of recording, classifying and summarizing in a significant manner and in terms of money, transactions and events which are in part at least of a financial character and interpreting the result thereof."

Thus accounting is the art of recording,classifying,summerising,analysing and interpreting the financial transaction and communicating the result thereof to the persons interested in such information

- Recording
- Classifying
- Summarizing
- Interpreting

Accounting Principles

Accounting principles may be defined as "those rules of conduct or procedure which are adopted by the accountants universally, while recording the accounting transactions."

Accounting principles are the body of doctrines commonly associated with the theory and procedure of accounting. It is a general law or rules adopted as a guide to action.

The accounting principles can be classified into two categories:

1. Accounting Concepts.

II. Accounting Conventions.

Accounting Concepts.

Accounting concepts mean and include necessary assumptions or postulates or ideas which are used to accounting practice and preparation of financial statements. The following are the important accounting concepts:

(1) Entity Concept; (2) Dual Aspect Concept;

(3) Accounting Period Concept; (4) Going Concern Concept;

(5) Cost Concept; (6)Money mesurement concept;

(7)Matching concept; (8)Realization concept;

(9)Accrual concept; (10)Rupee value concept;

Accounting Conventions

Accounting Convention implies that those customs. Accountants have to adopt these usages and customs which are termed as conventions in acconting.in order to have universal acceptance, methods and practices to be followed as a guideline

for preparation of accounting statements. The accounting conventions can be classified as follows:

(1) Convention of Disclosure (2) Convention of Conservatism.

(3) Convention of Consistency. (4) Convention of Materiality.

Accounting Concepts

(1) Entity Concept:

Separate entity concept implies that business unit or a company is a body corporate and having a separate legal entity distinct from its proprietors. As per the separate entity concept of accounting it applies to all forms of business to determine the scope of what is to be recorded or what is to be excluded from the business books

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(2) Dual Aspect Concept:

According to this concept, every business transaction involves two aspects, namely, for every receiving of benefit and there is a corresponding giving of benefit. The dual aspect concept is the basis of the double entry book keeping. Accordingly for every debit there is an equal and corresponding credit.

The accounting equation of the dual aspect concept is:

Capital + Liabilities = Assets

(or)

Assets Equities (Capital)

(3) Accounting Period Concept:

According to this concept, income or loss of a business can be analysed and determined on the basis of suitable accounting period instead of wait for a long period, Le., until it is liquidated. Thus, the accounting period is normally adopted for one year.

This concept is simply intended for a periodical ascertainment and reporting the true and fair financial position of the concern as a whole.

(4) Going Concern Concept:

It is otherwise known as Continue of Activity Concept. This concept assumes that business concern will continue for a long period to exit. In other words, under this assumption, the enterprise is normally viewed as a going concern and it is not likely to be liquidated in the near future. It is useful in valuation of assets and liabilities, depreciation of fixed assets and treatment of prepaid expenses.

(5) Cost Concept:

This concept is based on "Going Concem Concept." Cost Concept implies that assets acquired are recorded in the accounting books at the cost or price paid to acquire it. And this cost is the basis for subsequent accounting for the asset. For accounting purpose the market value of assets are not taken into account either for valuation or charging depreciation of such assets.

(6) Money Measurement Concept:

According to this concept, accounting transactions are measured,expressed and recorded in terms of money. This concept excludes

those transactions or events which cannot be expressed in terms of money. For example, factors such as the skill of the supervisor, product policies, planning, employer-employee relationship cannot be recorded in accounts in spite of their importance to the business. This makes the financial statements incomplete.

(7) Matching Concept:

Matching Concept is closely related to accounting period concept.The chief aim of the business concern is to ascertain the profit periodically. To measure the profit for a particular period it is essential to match accurately the costs associated with the revenue. Thus,matching of costs and revenues related to a particular period is called as Matching Concept.

(8) Realization Concept:

Realization Concept is otherwise known as Revenue Recognition Concept. According to this concept, revenue is the gross inflow of cash, receivables or other considerations arising in the course of an enterprise from the sale of goods or rendering of services from the holding of assets. If no sale takes place, no revenue is considered. However, there are certain exceptions to this concept. Examples, Hire Purchase/ Sale, Contract Accounts etc.

(9)Accrual Concept:

Accrual Concept is closely related to Matching Concept. According to this concept, revenue recognition depends on its realization and not accrual receipt. Likewise cost are recognized when they are incurred and not when paid. The accrual concept ensures that the profit or loss shown is on the basis of full fact relating to all expenses and incomes.

(10) Rupee Value Concept:

This concept assumes that the value of rupee is constant. In fact, due to inflationary pressures, the value of rupee will be declining. Under this situations financial statements are prepared on the basis of historical costs not considering the declining value of rupee. Similarly depreciation is also charged on the basis of cost price.

Accounting Conventions

(1) Convention of Disclosure:

The disclosure of all material information is one of the important accounting conventions. According to this conventions all accounting statements should be honestly prepared and all facts and figures must be disclosed therein. The disclosure of financial informations are required for different parties who are interested in the welfare of that enterprise.

(2)Convention of Conservatism:

This convention is closely related to the policy of playing safe.This principle is" often described as "anticipate no profit, and provide for all possible losses." Thus, this convention emphasise that uncertainties and risks inherent in business transactions should be given proper consideration. For example, under this convention inventory is valued at cost price or market price whichever is lower. Similarly, bad and doubtful debts is made in the books   ascertaining the profit.

(3) Convention of Consistency:

The Convention of Consistency implies that accounting policies,procedures and methods should remain unchanged for preparation of financial statements from one period to another. Under this convention alternative improved accounting policies are also equally acceptable. In order to measure the operational efficiency of a concern, this convention allows a meaningful comparison in the performance of different period.

(4) Convention of Materiality:

According to this convention consideration is given to all material events, insignificant details are ignored while preparing the profit and loss account and balance sheet. The evaluation and decision of material or immaterial depends upon the circumstances and lies at the discretion of the Accountant.

Accounting standards

Meaning of Accounting Standards:

Accounting Standards are written policy documents issued by expert accounting body or by the government or other regulatory body covering the aspects of recognition, measurement, treatment, presentation, and disclosure of accounting transactions in financial statements.

Accounting is considered the language of business . Each language has certain set of rules. Similarly , accounting has certain rules to be observed by the accountants so that it is understood by all in the same sense. These set of rules become

accounting standards when a proffesional body codifies and insists them while recording and reporting facts about the business. Thus accounting standards are certain set of rules and guidlines based on the principles and methods of accounting to be followed to have uniformity in terminology , approach and presentation of results.

Accounting Standards mainly deal with four major issues of accounting,namely

- Recognition of financial events
- Measurement of financial transactions
- Presentation of financial statements in a fair manner
- Disclosure requirement of companies to ensure stakeholders are not misinformed

Objective of Accounting Standards defined by ICAI

- To provide a standard for the diverse accounting policies and principles.
- To put an end to the non-comparability of financial statements.
- To increase the reliability of the financial statements.
- To provide standards which are transparent for users.
- To define the standards which are comparable over all periods presented.
- To provide a suitable starting point for accounting.
- It contains high quality information to generate the financial reports. This can be done at a cost that does not exceed the benefits.
- For the eradication the huge amount of variation in the treatment of

Benefits of Accounting Standards

- Attains Uniformity in Accounting
- Improves Reliability of Financial Statements
- Prevents Frauds and Accounting Manipulations
- Assists Auditors
- Comparability
- Determining Managerial Accountability

Limitations of Accounting Standards

• it makes choice between different alternate treatement which are difficult to apply

• it is high rigid and hence not flexible in applying accounting standards
•it cannot override the prevailing status

Applicability of Accounting standards

1. sole proprietorships
2. Partnerships
3. Societies
4. Trusts
5. Hindu undivided families

6. Association of persons
7.co-operative societies
8.companies
9.international financial reporting system

ACCOUNTING STANDARDS 2021

AS 1 Disclosure of Accounting Policies

AS2 Valuation of Inventories

AS 3 Cash Flow Statements

AS 4 Contingencies and Events Occurring After the Balance Sheet Date

AS 5 Net Profit or Loss for the Period, Prior Period Items and Changesin Accounting Policies

AS 6 depreciation accounting

AS 7 Construction Contracts

AS 8 Research and Development

AS 9 Revenue Recognition

AS 10 Property, Plant and Equipment

AS 11 The Effects of Changes in Foreign Exchange Rates

AS 12 Accounting for Government Grants

AS 13 Accounting for Investments

AS 14 Accounting for Amalgamations

AS 15 Employee Benefits

AS 16 Borrowing Costs

AS 17 Segment Reporting

AS 18 Related Party Disclosures

AS 19 Leases

AS 20 Earnings Per Share

AS21 Consolidated Financial Statements

AS 22 Accounting for Taxes on Income

AS 23 Accounting for Investments in Associates in Consolidated Financial Statements

AS 24 Discontinuing Operations

AS 25 Interim Financial Reporting

AS 26 Intangible Assets

AS 27 Financial Reporting of interests in Joint Ventures

AS 28 Impairment of Assets

AS 29 Provisions, Contingent Liabäties and Contingent Assets