CHAPTER - 1

INTRODUCTION OF FINANCIAL ACCOUNTING

DEFINITION OF ACCOUNTING

- According to American Institute of Certified Public Accountants (AICPA) "Accounting is 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 results thereof ".

PROCESS OF ACCOUNTING

- **RECORDING TRANSACTIONS**
- **CLASSIFYING THE TRANSACTIONS**
- **SUMMARISING THE TRANSACTIONS**
- **INTERPRETING THE TRANSACTIONS**
- **COMMUNICATION OF RESULTS**

OBJECTIVES / NEED / ADVANTAGES / IMPORATANCE OF ACCOUNTING

- **SYSTEMATISES RECORDING OF TRANSACTIONS**
- **ASCERTAINMENT OF RESULT OF ABOVE RECORDED TRANSACTIONS**
- **ASCERTAINMENT OF THE FINANCIAL POSITION OF THE BUSINESS**
- **PROVIDING INFORMATION TO THE USERS FOR RATIONAL DECISION MAKING**
- **TO KNOW THE SOLVENCY POSITION**

FUNCTIONS OF ACCOUNTING

1. **MEASUREMENT**

2. **FORECASTING**

3. **DECISION – MAKING**

4. **COMPARISON AND EVALUATION**

5. **CONTROL**
6. **GOVERNMENT REGULATION AND TAXATION**

LIMITIATION / DISADVANTAGES / DEMERITS OF ACCOUNTING

1. **RECORDING ONLY MONETARY ITEMS**
2. **TIME VALUE OF MONEY**
3. **RECOMMENDATION OF ALTERNATIVE METHODS**
4. **ACCOUNTING PRINCIPLES**

5. RECORDING OF PAST EVENTS

6. ALLOCATION OF PROBLEM

7. MAINTAINING SECRECY

8. TENDENCY FOR SECRET RESERVES

USERS OF ACCOUNTING INFORMATION

- Owners
- Management
- Investors
- Creditors
- Employees
- Government
- Customers
- Investment agencies
- Stock exchange
- Economics
- General public

BRANCHES OF ACCOUNTING

- **FINANCIAL ACCOUNTING**

  Financial Accounting is based on a systematic method of recording transactions. It is the original form of the accounting process. The main purpose of financial accounting is to calculate Trial Balances, Profit & Loss Accounts and Balance Sheets. These are used by creditors, banks and financial institutions to assess the financial status of the company.

- **COST ACCOUNTING**

  Cost accounting deals with evaluating the cost of a product or service offered. The objective of cost accounting is to help the management in fixing the prices and controlling the cost of production. It also pin points any wastages, leakages and defects during manufacturing and marketing processes.

- **MANAGEMENT ACCOUNTING**

  It helps in making important decisions and controlling of various activities of the business. The management is able to take decisions efficiently with the help of various Management Information Systems such as Budgets, Cash Flow and Fund Flow Statements.

BASIS OF ACCOUNTING

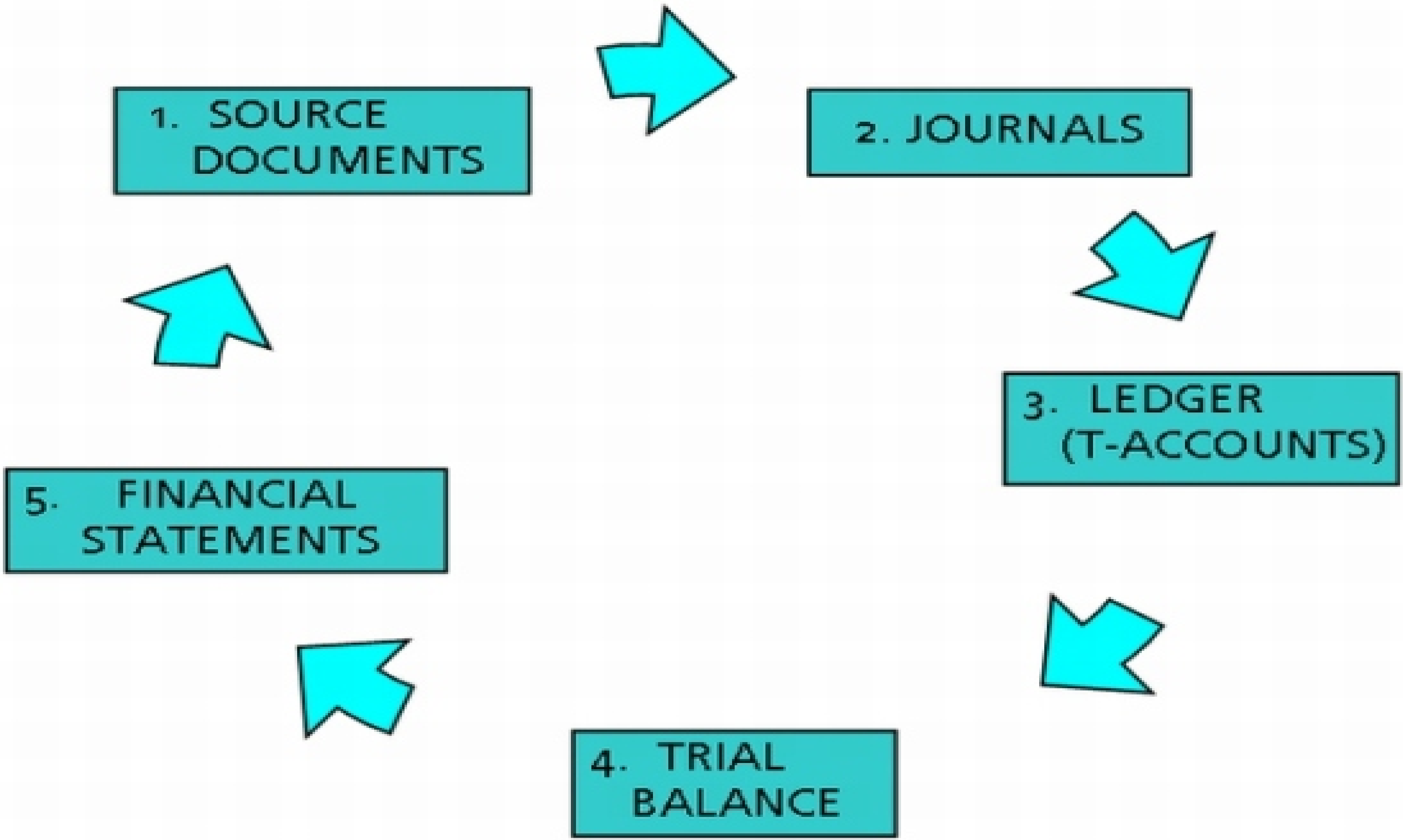
- **CASH BASIS OF ACCOUNTING**

  Under the basis of accounting, Revenue is recorded when cash is received . Expenses are recorded when cash is paid. It records only cash transactions.

- **ACCRUAL BASIS OF ACCOUNTING / MERCANTILE BASIS OF ACRUAL BASIS**

  Under the basis of accounting, revenue is recorded when it is earned. Expenses are recorded when incurred. It records both cash transactions and credit transactions.

ACCOUNTING CYCLE



- **CAPITAL :**

  Capital refers to investment made by owners of a business enterprise in the form of cash or kind.

- **DRAWINGS:**

  Drawings refers the money or any other item, if the business used or withdrawn by owners for personal purposes.

- **GOODS:**

  Goods refers to articles, commodities, things with which business deals. Example: stationery, books pens, pencils, table, cupboards.

- **PURCHASES:**

  Purchase refers to acquisition of goods,

- **PURCHASE RETURNS:**

  When goods purchased are returned to the supplier of goods on account of damage defect.

ACCOUNTING PRINCIPLES

Accounting Concepts

1. Money Measurement
2. Business Entity
3. Going Concern
4. Cost
5. Dual Aspect
6. Accounting Period
7. Matching
8. Realisation

Accounting Conventions

1. Disclosure
2. Consistency
3. Conservatism
4. Materiality

ACCOUNTING CONCEPTS

1. Business entity concept:

A business and its owner should be treated separately as far as their financial transactions are concerned.

2. Money measurement concept:

Only business transactions that can be expressed in terms of money are recorded in accounting, though records of other types of transactions may be kept separately.

3. Dual aspect concept:

Dual Aspect of Accounting means that every transaction that take place has two aspects one is debit & another is credit & because of dual aspect of a transaction asset side of Balance sheet matches with Liabilities side. The Accounting equation is : Liabilities + Capital= Assets

ACCOUNTING STANDARD

- An accounting standard is a set of principles, standards and procedures that define the financial accounting policies and practices. Accounting standards improve the transparency of financial reporting in all countries.

ADVANTAGES / IMPORTANCE OF ACCOUNTING STANDARDS

- Accounting standards help investors in judging for company.
- Accounting standards helps the chartered accountants to deal with their clients by providing rules and regulations
- Accounting standards helps in reporting financial statements
- Accounting standards helps the tax authorities and government officials.
- Accounting standards helps in reliable documents for the purpose of analysis and interpretation of data.

LIMITATIONS OF ACCOUNTING STANDARDS

- Accounting standards flexibility problem
- Accounting standards have to many rules and regulations.
- Difficulty in finding solutions