

Chp-1. Theoretical Framework

Unit 1: Meaning & Scope of Accounting.

(1) Accounting

⇒ Accounting is an art of recording, classifying & summarising in a significant manner & in terms of money, transactions & events which are, in part at least, of a financial character, & interpreting the result thereof.

recording → Journal [Book of original entry]

Ex. (i) Purchase book.

(ii) Sales book.

(iii) Purchase Return book.

(iv) Sales Return book.

(v) Bills Receivable book.

(vi) Bills Payable book.

(vii) Cash book.

(viii) Journal proper.

classifying → Ledger [Principal book]

summarising → Trial Balance

★ transactions & events → result of transaction.

↓

Ex. (i) Profit or Loss.

Performance of an act.

(ii) Closing Inventory left.

Ex. (i) Purchase / Sale of goods.

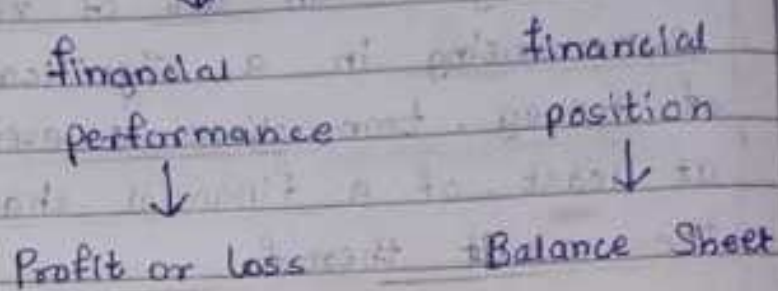
(ii) Capital Investment.

(iii) Expenses Incurred.

* ①. Purchase or Sale of Fixed Assets.
→ Transaction & event both.

financial character → related to Business.

interpreting the result → to find the conclusion



② Functions of Accounting

[these are given by Accounting Principle Board (APB) & American Institute of Certified Public Accountant (AICPA).]

(i) Recording — Journal

(ii) Classifying — Ledger

(iii) Summarising — Trial Balance

(iv) Analysis & Interpretation — Analysing the result.

(v) Communicating to the user.

③ Objectives of Accounting

- (i) Systematic recording of transactions.
- (ii) Ascertainment of results & financial position.
- (iii) Providing information to users for rational decision making.
- (iv) To know the solvency position.

④ Evolution of Accounting

- (i) As early as 4000 B.C [Egyptians].
- (ii) Romans used to prepare day books, where receipts & payments were recorded [700 B.C to 400 AD].
- (iii) Kautilya [Minister in Chandragupta's Kingdom] wrote book named Arthashastra.
- (iv) 1494 — Double Entry Book Keeping [first book] written by the father of Accounting Luca Pacioli [Venice].
- (v) Debit — It comes from Italian word 'Debito' which comes from Latin word 'Debita' [owed to the proprietor].

Credit — It comes from Italian word 'Credito' which comes from Latin word 'Credo' [belief / trust in proprietor].

(vi) Stewardship Accounting — root of financial accounting system.

⑤ Sub fields of Accounting

(i) Financial Accounting → To ascertain profit or loss.

(ii) Management Accounting → It helps the management in decision making.

(iii) Cost Accounting → To ascertain cost of product & it helps in fixation of price.

(iv) Social ^{Responsibility} Reporting Accounting → Social cost and social benefits.

(v) Human Resource Accounting → Reporting investment in human resources.

⑥ Functions of Accounting

[Imp. & it is different from point ②]

(i) Measurement — It measures the past performance of the business.

(ii) Forecasting — It helps in forecasting future performance using past data.

(iii) Decision Making — It provides relevant information to the users to help them in decision making.

(iv) Comparison & Evaluation — It provides basis for comparison [inter firm or inter firm] and evaluates result.

(v) Control — It identifies weakness in the operational system of the business.

(vi) Government Regulation & Taxation — It provides necessary information to the government & helps in collection of taxes.

(7) Limitations of Accounting

(i) Accounting is not fully exact as it is based on estimation (guess). Ex, Provision for doubtful debts.

(ii) Accounting ignores Qualitative aspects.

(iii) Accounting ignores price level changes.

(iv) There are occasions when accounting principles conflict with each other.

(v) Window Dressing + Manipulation in books of accounts.

(8) Book-Keeping

⇒ Book-keeping is an activity concerned mainly with recording of financial data relating to business operations in a significant and orderly manner.

⇒ Objectives of Book-Keeping

- (i) Complete recording of transactions.
- (ii) Ascertainment of financial effect on the business.

⇒ Book-Keeping and Accounting

Book-Keeping	Accounting
(i) It is concerned with <u>recording</u> the transactions.	It is concerned with <u>summarising</u> the recorded transaction.
(ii) It is a <u>primary</u> stage.	It is a <u>secondary</u> stage i.e., it begins when book keeping ends.
(iii) Financial statements do not form part of this process.	Financial statements are prepared in this process.
(iv) There is <u>no</u> sub-field of book keeping.	(v) There are <u>sub-fields</u> of accounting.
(vi) Managerial <u>decisions</u> can be taken on this basis.	Managerial <u>decisions</u> can be taken on its basis.
(vii) It is performed by junior staff [which requires <u>no specialised skills</u>].	It is performed by senior staff [which requires <u>specialised skills</u>].

Accountancy

Accounting

Book-Keeping

→ Principle of Accounting

⑨ Users of Accounting Information

- (i) Internal users - access to the information.
i.e. Board of Directors, Partners, Managers, Officers.
- (ii) External users - do not have access to the information
i.e. Investors, Lenders, Suppliers, Govt. agencies, Customers, Creditors.

⑩ Relationship of Accounting with other disciplines / Subject

(i) Accounting & Economics

→ Accounting is a system, which provides data to users to help them in decision making.

→ Economics is viewed as science of rational decision making.

^{gulf-difference} → However, there exists a wide gulf ~~between~~ between economist's and accountants' ~~concept~~ ^{of} concept of capital and income.

→ At the macro level, accounting provides the data base over which economic decision models have been developed.

(ii) Accounting & Statistics

→ The use of statistics in accounting can be appreciated better in the context of the nature of accounting records.

→ In accounts, all the values are important individually because they relate to business. However, in statistics values are represented as an aggregate.

→ In accountancy, number of financial and other ratios are based on statistical methods. Statistical methods are helpful in developing accounting data & its interpretation.

(iii) Accounting & Mathematics

→ Knowledge of Arithmetic and Algebra is a prerequisite for accounting computations. [Ex. interest, annuity, etc.]

→ In modern era, many accounting transactions are recorded in the matrix form.

→ Presently graphs and charts are also used for communicating accounting information.

(iv) Accounting & Law

→ Provisions are there and accounting is done on the basis of these provisions [IPA, 1932].

(v) Accounting & Management

→ Accounting information helps the management in decision making.

(11) Role of Accountant in the Society

- (i) Maintenance of Books of Accounts.
- (ii) Statutory Audit - financial statements of the business should be true or fair view.
- (iii) Internal Audit - It is a management tool whereby internal auditor examines the accounting transactions.
- (iv) Taxation - Direct [Income Tax] & Indirect [GST].
- (v) Management Accounting & Consultancy Service
- (vi) Financial Advice - related to insurance, investments, business expansions, investigations, pension schemes, etc.
- (vii) Other services - secretarial work, share registration work, company formation, arbitrations [settle a dispute], cost accountants, etc.

* Chartered Accountant

- (i) In Industry - rebudgeting, cost accounting, taxation, management accounting.
- (ii) In Public Sector Enterprises - CA prepares accounts & reports of these enterprises.
- (iii) In framing fiscal policies - CA has important role in determination of fiscal policies (related to income and expenses).

(iv) In economic growth - They help in increasing business efficiency.