**UCC 200 LECTURE NOTES**

**ASSETS, LIABILITIES, REVENUES, EXPENSES, THE ACCOUNTING CYCLE, THE CONCEPTUAL FRAMEWORK OF ACCOUNTING**

**Assets**

**A**n asset can be defined as resources present in a business organization that have probable future economic benefit. They include cash, land and buildings stock e.t.c.

Assets can either be defined as current, non-current or intangible.

**Current Assets:** these are assets consumed in one year or are expected to benefit the firm within a period of not more than one financial year e.g. stock, cash at hand, cash at bank, debtors, prepayments e.t.c

**Non-current Assets:** these are assets whose economic benefits to the organization are achieved

for a period exceeding one financial year. Examples would be land and buildings, motor vehicles, plant and machinery, computers e.t.c

**Intangible Assets:** these are assets of economic value to the business enterprise but cannot be

physically felt or seen e.g. goodwill, patents, copyrights e.t.c

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**Liabilities**

These are obligations that a business is expected to meet within a certain duration. They can also be defined as total funds owed for assets supplied to a business or expense incurred but not paid yet. Liabilities can either be short term or long term.

**Short term liabilities** are those that are expected to be met within duration of one financial year. e.g Payment for accrued expense, creditors, dividends to share holders e.t.c.

**Long term liabilities** are those payable within a period exceeding one financial year e.g. long term loan, re-payment of debentures e.t.c

**Capital:** this is defined as the total of all resources invested and left in business by its owner.

**Revenue/Income**: this can be defined as the monetary value of all goods and services sold to

customers by a business enterprise

**Expenses:** This can be defined as the monetary equivalent of all resources/assets that have been consumed during a given period to generate the revenues for the business organization in a given accounting period.

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**THE ACCOUNTING CYCLE**

The accounting process can be perceived as a cycle which starts with the occurrence of a transaction, recording of the transaction and finally the preparation of the financial statements.

Financial statements are reports on results of all the transactions that occur during the year and the position of the business as at the last date of the accounting period. A transaction is an activity which involves the exchange of goods and services for another thing of value e.g. when the business purchases goods for sale, sells goods to customers on credit, pays for services e.g. telephone.

A transaction is first recorded in the source documents e.g. the cash sale receipt, the invoices

received from creditors, debit and credit notes issued and received etc. The daybooks as the name suggests they are filled daily showing all the transactions that occurred during the day. Such information is obtained from the source documents. The data in the day books is then filled in the ledger accounts and a trial balance extracted as the end of the accounting period. Adjustments e.g. for prepayments and accruals are then made and an adjusted trial balance is drawn reflecting these changes.

From this trial balance, the final statements are prepared i.e. the statement of comprehensive

income which reveals whether the company made a profit or loss from the transactions carried

out in the year, and the statement of financial position which tells of the financial position of the business in terms of its assets and liabilities as at that closing date. After these, the closing entries are made to prepare the accounts to receive the data for the following financial period and a closing trial balance extracted. This marks the end of journals. For every transaction entered into the business enterprise, there is the primary book where it will be initially recorded. This is known as books of original entry.

**THE CONCEPTUAL FRAMEWORK OF ACCOUNTING**

The conceptual framework is a body of interrelated objectives and fundamentals. The objectives identify the goals and purposes of financial accounting and the fundementals are the underlying concepts that help achieve those objectives. Those concepts provide guidance in selecting transactions, events and circumstances to be accounted for, how they should be recognized and measured and how they should be summarized and reported.

**FUNDAMENTAL ACCOUNTING CONCEPTS**

Fundamental accounting concepts are broad general assumptions which underline the periodic financial statements of business enterprises. The following are the important accounting concepts and conventions

1. Separate Business Entity Concept

2. Money Measurement Concept

3. Dual Aspect Concept

4. Going Concern Concept

5. Accounting Period Concept

6. Cost Concept

7. The Matching Concept

8. Accrual Concept

9. Realisation Concept

1. Separate Business Entity Concept

In accounting we make a distinction between business and the owner. All the books of accounts records day to day financial transactions from the view point of the business rather than from that of the owner. The proprietor is considered as a creditor to the extent of the capital brought in business by him. For instance, when a person invests money into a business, it will be treated that the business has borrowed that much money from the owner and it will be shown as a ‘liability’ in the books of accounts of business. Similarly, if the owner of a business take cash from the cash box for meeting certain personal expenditure, the accounts would show that cash had been reduced even though it does not make any difference to the owner himself. Thus, in recording a transaction the important question is how does it affects the business? For example, if the owner puts cash into the business, he has a claim against the business for capital brought in.

2. Money Measurement Concept

In accounting, only those business transactions are recorded which can be expressed in terms of money. In other words, a fact or transaction or happening which cannot be expressed in terms of money is not recorded in the accounting books. As money is accepted not only as a medium of exchange but also as a store of value, it has a very important advantage since a number of assets and equities, which are otherwise different, can be measured and expressed in terms of a common denominator.

3. Dual Aspect Concept

Financial accounting records all the transactions and events involving financial element. Each of such transactions requires two aspects to be recorded. The recognition of these two aspects of every transaction is known as a dual aspect analysis. According to this concept every business transactions has dual effect. For example, if a firm sells goods of sh 5,000 this transaction involves two aspects. One aspect is the delivery of goods and the other aspect is immediate receipt of cash (in the case of cash sales). In fact, the term ‘double entry’ book keeping has come into vogue and in this system the total amount debited always equals the total amount

4. Going Concern Concept

Accounting assumes that the business entity will continue to operate for a long time in the future unless there is good evidence to the contrary. The enterprise is viewed as a going concern, that is, as continuing in operations, at least in the foreseeable future. In other words, there is neither the intention nor the necessity to liquidate the particular business venture in the predictable future

5. Accounting Period Concept

This concept requires that the life of the business should be divided into appropriate segments for studying the financial results shown by the enterprise after each segment. A year is the most common interval on account of prevailing practice, tradition and government requirements. Some firms adopt financial year of the government, some other calendar year. Although a twelve-month period is adopted for external reporting, a shorter span of interval, say one month or three month is applied for internal reporting purposes. All the revenues and all the cost relating to the year in operation have to be taken into account while matching the earnings and the cost of those earnings for the any accounting period.

6. Cost Concept

According to this concept an asset is ordinarily entered on the accounting records at the price paid to acquire it. For example, if a business buys a plant for sh 5 million, the asset would be recorded in the books at sh 5 millions even if its market value at that time happens to be sh 6 millions . Thus, assets are recorded at their original purchase price and this cost is the basis for all subsequent accounting for the business. The assets shown in the financial statements do not necessarily indicate their present market values.

7. The Matching concept

This concept is based on the accounting period concept. In reality we match revenues and expenses during the accounting periods. Matching is the entire process of periodic earnings measurement, often described as a process of matching expenses with revenues. In other words, income made by the enterprise during a period can be measured only when the revenue earned during a period is compared with the expenditure incurred for earning that revenue. Only costs that have expired during an accounting period are considered as expenses On account of this concept, adjustments are made for all prepaid expenses, outstanding expenses, accrued income, etc., while preparing periodic reports.

8. Accrual Concept

Accrual concept makes a distinction between the receipt of cash and the right to receive it, and the payment of cash and the legal obligation to pay it. This concept provides a guideline to the accountant as to how he should treat the cash receipts and the right related thereto. Accrual principle tries to evaluate every transaction in terms of its impact on the owner’s equity. The essence of the accrual concept is that net income arises from events that change the owner’s equity in a specified period and that these are not necessarily the same as change in the cash position of the business. Thus, it helps in proper measurement of income.

9. Realisation Concept

According to realisation concept revenue is recognized when sale is made. Sale is considered to be made at the point when the property in goods passes to the buyer and he becomes legally liable to pay. This implies that revenue is generally realised when goods are delivered or services are rendered. The rationale is that delivery validates a claim against the customer. However, in case of long run construction contracts revenue is often recognised on the basis of a proportionate or partial completion method.