**FUNDAMENTAL ACCOUNTING ASSUMPTIONS OR CONCEPTS**

**The Fundamental Accounting Assumptions are:**

1. **Going Concern Assumption**
2. **Consistency Assumption ; and**
3. **Accrual Assumption.**
4. **Going Concern Assumption:** According to this assumption, it is assumed that business shall continue for a foreseeable period and there is no intention to close the business or scale down its operations significantly. This implies that it will not be dissolved in the immediate future unless there is a clear evidence of closure. It is because of this concept that a distinction is made between a capital expenditure, i.e. expenditure that will give benefit for a long period and revenue expenditure.
5. **Consistency Assumption:** According to the Consistency Assumption, accounting practices once selected and adopted, should be applied consistently year after year .The concept helps in better understanding of accounting information and makes it comparable ( a qualitative characteristic of accounting information) with that of previous years. Consistency eliminates personal bias and helps in achieving results that are comparable.
6. **Accrual Assumption:** According to the Accrual Assumption, a transaction is recorded in the books of accounts at the time when it is entered into and not when the settlement takes place. Thus, revenue is recognised when it is realised, i.e. when sale is complete or services are rendered; it is immaterial whether cash is received or not. Similarly, expenses are recognised as expenses in the accounting period in which the revenue related to it is recognised, whether paid in cash or not.

**Sale of goods Rs 25,000 and cash received 5,000.**

Sales (Income) – Rs 25,000

Cash – Rs 5,000

Debtors – Rs 20,000

**ACCOUNTING PRINCIPLES:**

1. **Accounting Entity or Business Entity Principle (concepts):** According to the Business Entity Principle, business is considered to be separate and distinct from its owners. Business transactions, therefore, are recorded in the books of accounts from the business point of view and not from that of the owners. Owners being recorded as separate and distinct from business they are considered creditors of the business to the extent of their capital. Their account with the business is credited with the capital introduced and profit earned during the year, etc. and debited by the drawings made. For example, when the proprietor introduces capital, Cash Account or Bank Account is debited and Capital Account is credited.
2. **Money Measurement Principle:** According to the Money Measurement Principle, transactions and events that can be measured in money terms are recorded in the books of accounts of the enterprise. In other words, money is the common denominator in recording and reporting all transactions. Consider that an enterprise has Rs 10,000 cash, 6 tonnes of raw material, 6 trucks and 10,000 sq. yards land.
3. **Accounting Period Principle:** According to the Accounting Period Principle, the life of an enterprise is broken into smaller periods so that its performances are measured at regular intervals. The accounts of an enterprise are maintained following the going concern concept, meaning the enterprise shall continue its activities for a foreseeable future. One may argue that the financial statements of the enterprise should be prepared at the end of its life. It is possible to do so, but a number of users of Financial Statements and many of them.

**Accounting period may be 1 year.**

1. **Full Disclosure Principle:** According to the Principle of Full Disclosure “there should be complete and understandable reporting on the financial statements of all significant information relating to the economic affairs of the entity.” Apart from legal requirements, goodaccounting practices requires all material and significant information to be disclosed.
2. **Materiality Principle**: The Materiality Principle refers to the relative importance of an item or an event. According to the American Accounting Association, “an item should be regarded as material if there is a reason to believe that knowledge of it would influence the decision of an informed investor.” Thus, whether an item is material or not will depend on its nature and/or amount.
3. **Prudence or Conservatism Principle:** The Prudence Principle is many a time described using the phrase “Do not anticipate a profit, but provide for all possible losses.” In other words, it takes into consideration all prospective losses but not the prospective profits. The application of this concept ensures that the financial statements present a realistic picture of the state of affairs of the enterprise and do not paint a better picture than what it actually is. For example, closing stock is valued at lower of cost or net realisable value or making the provision for doubtful debts and discount on debtors in anticipation of actual bad debts and discount.
4. **Cost Concept or Historical Cost Principle**: According to the Cost Concept, an asset is recorded in the books of accounts at the price paid to acquire it and the cost is the basis for all subsequent accounting of the asset. Asset is recorded at cost at the time of its purchase but is systematically reduced in value by charging depreciation. The market value of an asset may change with the passage of time but for accounting purposes it continues to be shown in the books of accounts as its book value (i.e. cost at which it was purchased minus depreciation provided up-to-date). For example, an asset is purchased for Rs 5,00,000 and if at the time of preparing the final accounts. Even if its market value is say Rs 4,00,000 or Rs 7,00,000, yet the asset shall be recorded as its purchase price of Rs 5,00,000.
5. **Matching Concept or Matching Principle**: This concept is based on the accounting period concept. An important objective of business is to determine profit periodically. It is necessary to match “revenues” of the period with the ‘expenses’ of that period to determine correct profit (or loss) for the accounting period. Profit earned by the business during a period can be correctly measured only when the revenue earned during the period is matched with the expenditure incurred to earn that revenue. It is not relevant when the payment was made or received. Therefore, as per this concept, adjustments are made for all outstanding expenses, prepaid expenses, accrued income, unearned income, etc.

Profit = Revenue (total income) - expenses

Loss = Expenses- Revenue

1. **Dual Aspect or Duality Principle**: According to the Dual Aspect Concept, every transaction entered into by an enterprise has two aspects, a debit and a credit of equal amount. Simply stated, for every debit there is a credit of equal amount in one or more accounts. It is also true vice versa. For example, Rahul starts a business with a capital of Rs 1,00,000. There are two aspects to the transaction. On one hand, the business has an asset of Rs 1,00,000 (cash) while on the other hand, it has a liability towards Rahul of Rs 1,00,000 (capital of Rahul). Thus, we can say

Capital (Equities) = Cash (Asset)

Rs 1,00,000= Rs 1,00,000

Suppose further, the enterprise borrows amount from a bank; its asset will increase but this will mean that out of the total assets, amount equal to borrowing is payable to the outsiders.

Duality = Double side

Purchase of Furniture Rs 50,000

Debit Credit

1. **Revenue Recognition Concept**: According to the Revenue Recognition Concept, revenue is considered to have been realised when a transaction has been entered into and the obligation to receive the amount has been established. It is to be noted that recognising revenue and receipt of an amount are two separate aspects. Let us take an example to understand it. An enterprise sells goods in February 2013 and receives the amount in April 2013. Revenue of this sales should be recognised in February 2013, i.e. when the goods are sold.
2. **Verifiable Objective Concept**: The Verifiable Objective Concept holds that accounting should be free from personal bias. Measurements that are based on verifiable evidences are regarded as objectives. It means all accounting transactions should be evidenced and supported by business documents. These supporting documents are cash memo, invoices, sales bills, etc., and they provide the basis for accounting and audit.

**ACCOUNTING STANDARDS**

The rise is diversity, complexity and globalisation of business made the study of accounting information essential. But the diversity in the accounting policies being followed and the accounting treatment of transactions and events made the accounting information less meaningful and also incomparable. A need was thus felt that certain minimum standards should be universally applicable, so that the accounting statements have the qualitative characteristics of reliability, relevance, understand ability and comparability.

# objectives of Accounting Standards:

1. Promote better understanding of Financial statements
2. Facilitating meaningful comparison of Financial statements of two or more entities.

# IFRS- International Financial Reporting Standards

**Rules of Dr. And Cr.**