Users of Accounting Information

The accounting process provides financial data for a broad range of individuals whose objectives in studying the data vary widely. Three primary users of accounting information were previously identified, Internal users, External users, and Government/ IRS. Each group uses accounting information differently, and requires the information to be presented differently.

<u>Internal Users</u>

Accounting supplies managers and owners with significant financial data that is useful for decision making. This type of accounting in generally referred to as managerial accounting.

Some of the ways internal users employ accounting information include the following:

- Assessing how management has discharged its responsibility for protecting and managing the company's resources
- Shaping decisions about when to borrow or invest company resources
- Shaping decisions about expansion or downsizing

<u>External Users</u>

Typically called financial accounting, the record of a business' financial history for use by external entities is used for many purposes. The external users of accounting information fall into six groups; each has different interests in the company and wants answers to unique questions. The groups and some of their possible questions are:

- **Owners and prospective owners.** Has the company earned satisfactory income on its total investment? Should an investment be made in this company? Should the present investment be increased, decreased, or retained at the same level? Can the company install costly pollution control equipment and still be profitable?
- **Creditors and lenders.** Should a loan be granted to the company? Will the company be able to pay its debts as they become due?
- **Employees and their unions.** Does the company have the ability to pay increased wages? Is the company financially able to provide long-term employment for its workforce?

- **Customers.** Does the company offer useful products at fair prices? Will the company survive long enough to honor its product warranties?
- **Governmental units.** Is the company, such as a local public utility, charging a fair rate for its services?
- **General public.** Is the company providing useful products and gainful employment for citizens without causing serious environmental problems?

Some of the ways external users employ accounting information include the following:

- Stockholders have the right to know how a company is managing its investments
- Federal and State Governments require tax returns and other documents often prepared by accountants
- Banks or lending institutions may use accounting information to guide decisions such as whether to lend or how much to lend a business
- Investors will also use accounting information to guide investment decisions

What Is a Trading Account?

A trading account can be any investment account containing securities, cash or other holdings. Most commonly, trading account refers to a day trader's primary account. These investors tend to buy and sell assets frequently, often within the same trading session, and their accounts are subject to special regulation as a result. The assets held in a trading account are separated from others that may be part of a long-term buy and hold strategy.

A trading account is an investment account. For the most part, however, it refers to an account used to trade securities.

A trading account can hold securities, cash and other investment vehicles just like any other brokerage account. The term can describe a wide range of accounts, including tax-deferred retirement accounts. In general, however, a trading account is distinguished from other investment accounts by the level of activity, purpose of that activity and the risk it involves.

What Is a Balance Sheet?

A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating its capital structure. It is a financial statement that provides a snapshot of what a company owns and owes, as well as the amount invested by shareholders.

- A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity.
- The balance sheet is one of the three (income statement and statement of cash flows being the other two) core financial statements used to evaluate a business.
- The balance sheet is a snapshot, representing the state of a company's finances (what it owns and owes) as of the date of publication.
- Fundamental analysts use balance sheets, in conjunction with other financial statements, to calculate financial ratios.

Definition of the Finance Function:

There are three ways of defining the finance function. Firstly, the finance function can simply be taken as the task of providing funds needed by an enterprise on favourable terms, keeping in view the objectives of the firm.

This means that the finance function is solely concerned with the acquisition (or procurement) of short- term and long-term funds.

More info - https://www.managementstudyhq.com/financial-function-types-importance-objectives.html

What Is the Time Value of Money (TVM)?

The time value of money (TVM) is the concept that money you have now is worth more than the identical sum in the future due to its potential earning capacity. This core principle of finance holds that provided money can earn interest, any amount of money is worth more the sooner it is received. TVM is also sometimes referred to as present discounted value.

More info: https://www.investopedia.com/terms/t/timevalueofmoney.asp

What Is Working Capital?

Working capital, also known as net working capital (NWC), is the difference between a company’s current assets, such as cash, accounts receivable (customers’ unpaid bills) and inventories of raw materials and finished goods, and its current liabilities, such as accounts payable. Net operating working capital is a measure of a company's liquidity and refers to the difference between operating current assets and operating current liabilities. In many cases these calculations are the same and are derived from company cash plus accounts receivable plus inventories, less accounts payable and less accrued expenses.

More info: https://www.investopedia.com/terms/w/workingcapital.asp

https://corporatefinanceinstitute.com/resources/knowledge/modeling/working-capital-formula/

What do you mean by dividend decision?

The financial decision relates to the disbursement of profits back to investors who supplied capital to the firm. The term dividend refers to that part of profits of a company which is distributed by it among its shareholders.

It is the reward of shareholders for investments made by them in the share capital of the company. The dividend decision is concerned with the quantum of profits to be distributed among shareholders.

A decision has to be taken whether all the profits are to be distributed, to retain all the profits in business or to keep a part of profits in the business and distribute others among shareholders. The higher rate of dividend may raise the market price of shares and thus, maximize the wealth of shareholders. The firm should also consider the question of dividend stability, stock dividend (bonus shares) and cash dividend.

Explain factors affecting the dividend decision.

The following are the some major factors which influence the dividend policy of the firm.

1. Legal requirements

There is no legal compulsion on the part of a company to distribute dividend. However, there certain conditions imposed by law regarding the way dividend is distributed. Basically there are three rules relating to dividend payments. They are the net profit rule, the capital impairment rule and insolvency rule.

2. Firm's liquidity position

Dividend payout is also affected by firm's liquidity position. In spite of sufficient retained earnings, the firm may not be able to pay cash dividend if the earnings are not held in cash.

3. Repayment need

A firm uses several forms of debt financing to meet its investment needs. These debt must be repaid at the maturity. If the firm has to retain its profits for the purpose of repaying debt, the dividend payment capacity reduces.

4. Expected rate of return

If a firm has relatively higher expected rate of return on the new investment, the firm prefers to retain the earnings for reinvestment rather than distributing cash dividend.

5. Stability of earning

Finance Manager

If a firm has relatively stable earnings, it is more likely to pay relatively larger dividend than a firm with relatively fluctuating earnings.

A Finance Manager distributes the financial resources of a company, is responsible for the budget planning, and supports the executive management team by offering insights and financial advice that will allow them to make the best business decisions for the company.

Finance Manager duties and responsibilities of the job

As a crucial member of the finance team, a typical Finance Manager job description should include, but not be limited to:

- Collecting, interpreting and reviewing financial information
- Predicting future financial trends
- Reporting to management and stakeholders, and providing advice how the company and future business decisions might be impacted
- Producing financial reports related to budgets, account payables, account receivables, expenses etc.
- Developing long-term business plans based on these reports
- Reviewing, monitoring and managing budgets
- Developing strategies that work to minimise financial risk
- Analysing market trends and competitors

Role of Accountant

Role of an accountant is doing functions related to the collection, accuracy, recording, analysis, and presentation of a business, company or organization's financial operations. He also holds a number of administrative functions in the company. Statutory auditing, internal audit, taxation are some of the roles of accountant.

1.Maintenance of books of accounts

Role of Accountant is very crucial in maintaining systematic records of financial transactions in order to calculate the net profit or loss for an accounting period and the financial position of an entity as on a particular date.

Maintaining proper books of accounts in the manner required by law and accounting policies followed by the entity is important for the entity. The books of accounts of the entity also support the future planning of business operations.

2. Statutory Audit

Usually, a Chartered Accountant audits the books of the entities like Limited companies, firms etc. according to the law. He ensures that the entities prepare the financial statements in accordance with generally accepted accounting principles, standards, and legal considerations. He also ensures that the financial statements show a true and fair view of the financial position of an entity.

3. Internal Audit

Accountants, internal staff are engaged in an internal audit by large-sized entities (like listed companies, companies required to conduct an internal audit under any law etc.) to ensure that all the accounting transactions related to respective accounting year are recorded, classified and summarized in accordance with the accounting policies followed by the entity. It also enables management to check whether all the instructions given by it is followed or not.

4. Budgeting

Budgeting refers to the planning of various business activities, transactions before their occurrence. Accountants and management prepare various plans to balance their business incomes and expenses.

Actual results are compared with the budgeted to find out the variation if any. Role of accounting is very important while preparing the budget.

5. Taxation

Another very important role of the accountant is to plan the tax liabilities of an entity. Accountants are capable to manage the tax matters of an entity, file returns, make representations before tax authorities, and settle the tax liabilities of an entity under various laws. Various tax planning advice, investments etc services can be provided by accountants.

6. Investigation

The accountants also carry an investigation to ascertain the financial position of some parties. They perform this function either by themselves or by hiring external professionals.

However, external professionals are more preferable than the internal staff due to their independence, which enhances the confidentiality of investigation report.

7. Management advisory services

Reporting internal controls to management, long-term plans, advisory regarding the business operation of an entity are the major responsibilities of an accountant.

What Is Financial Reporting?

Financial reporting is the disclosure of financial results and related information to management and external stakeholders (e.g., investors, customers, regulators) about how a company is performing over a specific period of time.

Financial reports are usually issued on a quarterly and annual basis and include the following:

- **Balance Sheet or Statement of Financial Position** – reports on a company's assets, liabilities, and owners' equity at a given point in time, usually the end of a fiscal quarter or year.
- **Income Statement or Profit and Loss Report** – reports on a company's income, expenses, and profits over a period of time, such as a fiscal quarter or year. This includes sales and the various expenses incurred during the stated period.
- **Statement of Changes in Equity or Statement of Retained Earnings** – reports on the changes in equity of the company during the stated period, such as a fiscal quarter or year.
- **Cash Flow Statement** – reports on a company's cash flow activities, including its operating, investing, and financing activities. These are typically referred to as sources and uses of cash.

Accounting Principles

Obviously, if each business organisation conveys its information in its own way, we will have a babel of unusable financial data.

Personal systems of accounting may have worked in the days when most companies were owned by sole proprietors or partners, but they do not anymore, in this era of joint stock companies.

These companies have thousands of stakeholders who have invested millions, and they need a uniform, standardised system of accounting by which companies can be compared on the basis of their performance and value.

Therefore, accounting principles based on certain concepts, convention, and tradition have been evolved by accounting authorities and regulators and are followed internationally.

These principles, which serve as the rules for accounting for financial transactions and preparing financial statements, are known as the "*Generally Accepted Accounting Principles*," or GAAP.

The application of the principles by accountants ensures that financial statements are both informative and reliable.

It ensures that common practices and conventions are followed, and that the common rules and procedures are complied with. This observance of accounting principles has helped developed a widely understood grammar and vocabulary for recording financial statements.

However, it should be said that just as there may be variations in the usage of a language by two people living in two continents, there may be minor differences in the application of accounting rules and procedures depending on the accountant.

For example, two accountants may choose two equally correct methods for recording a particular transaction based on their own professional judgement and knowledge.

Accounting principles are accepted as such if they are (1) objective; (2) usable in practical situations; (3) reliable; (4) feasible (they can be applied without incurring high costs); and (5) comprehensible to those with a basic knowledge of finance.

Accounting principles involve both accounting concepts and accounting conventions. Here are brief explanations.

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:** For every credit, a corresponding debit is made. The recording of a transaction is complete only with this dual aspect.

4. **Going concern concept:** In accounting, a business is expected to continue for a fairly long time and carry out its commitments and obligations. This assumes that the business will not be forced to stop functioning and liquidate its assets at “fire-sale” prices.
5. **Cost concept:** The fixed assets of a business are recorded on the basis of their original cost in the first year of accounting. Subsequently, these assets are recorded minus depreciation. No rise or fall in market price is taken into account. The concept applies only to fixed assets.
6. **Accounting year concept:** Each business chooses a specific time period to complete a cycle of the accounting process—for example, monthly, quarterly, or annually—as per a fiscal or a calendar year.
7. **Matching concept:** This principle dictates that for every entry of revenue recorded in a given accounting period, an equal expense entry has to be recorded for correctly calculating profit or loss in a given period.
8. **Realisation concept:** According to this concept, profit is recognised only when it is earned. An advance or fee paid is not considered a profit until the goods or services have been delivered to the buyer.

Accounting Conventions

There are four main conventions in practice in accounting: conservatism; consistency; full disclosure; and materiality.

Conservatism is the convention by which, when two values of a transaction are available, the lower-value transaction is recorded. By this convention, profit should never be overestimated, and there should always be a provision for losses.

Consistency prescribes the use of the same accounting principles from one period of an accounting cycle to the next, so that the same standards are applied to calculate profit and loss.

Materiality means that all material facts should be recorded in accounting. Accountants should record important data and leave out insignificant information.

Full disclosure entails the revelation of all information, both favourable and detrimental to a business enterprise, and which are of material value to creditors and debtors.

Basic Accounting Terms

Here is a quick look at some important accounting terms.

Accounting equation: The accounting equation, the basis for the double-entry system (see below), is written as follows:

Assets = Liabilities + Stakeholders’ equity

This means that all the assets owned by a company have been financed from loans from creditors and from equity from investors. “Assets” here stands for cash, account receivables, inventory, etc., that a company possesses.

Accounting methods: Companies choose between two methods—cash accounting or accrual accounting. Under cash basis accounting, preferred by small businesses, all revenues and expenditures at the time when payments are actually received or sent are recorded. Under accrual basis accounting, income is recorded when earned and expenses are recorded when incurred.

Account receivable: The sum of money owed by your customers after goods or services have been delivered and/or used.

Account payable: The amount of money you owe creditors, suppliers, etc., in return for goods and/or services they have delivered.

Accrual accounting: See “accounting methods.”

Assets (fixed and current): Current assets are assets that will be used within one year.

For example, cash, inventory, and accounts receivable (see above). Fixed assets (non-current) may provide benefits to a company for more than one year—for example, land and machinery.

Balance sheet: A financial report that provides a gist of a company’s assets and liabilities and owner’s equity at a given time.

Capital: A financial asset and its value, such as cash and goods. Working capital is current assets minus current liabilities.

Cash accounting: See “accounting methods.”

Cash flow statement: The cash flow statement of a business shows the balance between the amount of cash earned and the cash expenditure incurred.

Credit and debit: A credit is an accounting entry that either increases a liability or equity account, or decreases an asset or expense account. It is entered on the right in an accounting entry. A debit is an accounting entry that either increases an asset or expense account, or decreases a liability or equity account. It is entered on the left in an accounting entry.

Double-entry bookkeeping: Under double-entry bookkeeping, every transaction is recorded in at least two accounts—as a credit in one account and as a debit in another.

For example, an automobile repair shop that collects Rs. 10,000 in cash from a customer enters this amount in the revenue credit side and also in the cash debit side. If the customer had been given credit, “account receivable” (see above) would have been used instead of “cash.” (Also see “single-entry bookkeeping,” below.)

Financial statement: A financial statement is a document that reveals the financial transactions of a business or a person. The three most important financial statements for businesses are the balance sheet, cash flow statement, and profit and loss statement (all three listed here alphabetically).

General ledger: A complete record of financial transactions over the life of a company.

Journal entry: An entry in the journal that records financial transactions in the chronological order.

Profit and loss statement (income statement): A financial statement that summarises a company's performance by reviewing revenues, costs and expenses during a specific period.

Single-entry bookkeeping: Under the single-entry bookkeeping, mainly used by small or businesses, incomes and expenses are recorded through daily and monthly summaries of cash receipts and disbursements. (Also see "double-entry bookkeeping," above.)

Types of accounting: Financial accounting reports information about a company's performance to investors and credits. Management accounting provides financial data to managers for business development.

Meaning of Financial Management

Financial Management means planning, organizing, directing and controlling the financial activities such as procurement and utilization of funds of the enterprise. It means applying general management principles to financial resources of the enterprise.

Objectives of Financial Management

The financial management is generally concerned with procurement, allocation and control of financial resources of a concern. The objectives can be-

1. To ensure regular and adequate supply of funds to the concern.
2. To ensure adequate returns to the shareholders which will depend upon the earning capacity, market price of the share, expectations of the shareholders.
3. To ensure optimum funds utilization. Once the funds are procured, they should be utilized in maximum possible way at least cost.
4. To ensure safety on investment, i.e, funds should be invested in safe ventures so that adequate rate of return can be achieved.
5. To plan a sound capital structure-There should be sound and fair composition of capital so that a balance is maintained between debt and equity capital.

Some numericals: https://www.studiestoday.com/dk-goel-accountancy-dk-goel-solutions-class-11-accountancy-financial-statement-304720.html

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