

**Accounting Concepts****Basis of preparation**

- The financial statements disclose basis of preparation in notes to the accounts.
- Refer live example “These financial statements have been prepared in accordance with the approved accounting standards ---IFRS and requirements of the Companies Ordinance 1984 “

**GOING CONCERN**

“ The enterprise is normally viewed as a going concern, that is, as continuing in operation for the foreseeable future. It is assumed that the enterprise has neither the intention nor the necessity of liquidation or of curtailing materially the scale of its operations.”

**ACCRUAL**

- Revenue and cost are recognized as they are earned or incurred respectively, not on the basis of money received or paid. In cash basis income is recorded on receipt basis and expenses are recorded when payment is made.
- All companies have to follow accrual basis of accounting but it is not disclosed rather it is assumed that these are prepared on accrual basis.

**CONSISTENCY**

- There are many areas in which judgment must be exercised in attributing money values. Like for charging depreciation we assume useful life of assets & for valuing inventories either LIFO or FIFO method is used.

**HISTORICAL COST CONCEPT**

- As basic principle of accounting is that transactions are normally stated in accounts at their historical amount.
- An important advantage of this procedure is that the objectivity of accounts is maximized. There is usually documentary evidence to prove the amount paid to purchase an asset or pay an expense. In general, accountants prefer to deal with costs, rather than with ‘values’.

### Post Balance Sheet Events

Events that occur between the balance sheet date and the date when the financial statements are authorised for issue. These events may be favourable or unfavourable.

#### EXAMPLES OF ADJUSTING EVENTS

- A court case existed at B/S date but settled after B/S date but before its issuance or a debtor become bad debts.
- Bankruptcy of a customer , providing for bad debts

#### EXAMPLE OF NON-ADJUSTING EVENTS

- Major purchases and disposal of assets
- The destruction of a major production plant

### CONTINGENCIES AND COMMITMENTS

- **Commitments** are business contractual obligation which company has entered into for future period, including future rental commitments under operating lease.
- A **contingency** is a condition or situation, the ultimate outcome of which gain or loss, will be confirmed only on the occurrence, or nonoccurrence, of one or more uncertain future events.
- A possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events **not** wholly within the control of the enterprise;
- PRACTICAL EXAMPLES : Siemens :: The company is contesting certain cases in the High Court of Sindh mainly relating to sales tax on advances from customers and installation sales revenue. The company's management and legal advisor are of the view that the cases have no factual sound legal footing and the final outcome of the cases will be in company's favour. Accordingly **no provision** has been made in the accounts against the demand raised by the Sales Tax Authorities.

### PRUDENCE

- Dictionary meanings: exercising good judgment or common sense.
- The other aspect of the prudence concept is that where a loss is foreseen, it should be anticipated and taken into account immediately, but expected income is not accounted for.

**DIVIDEND**

Dividends are distribution of profit that companies make to their shareholders.

Cash Dividend

Stock dividend

**Statement of Changes in Equity**

It provides movement in equity like capital injected through right shares or bonus shares issued from reserves , profit added or loss deducted and dividend paid out .It does not include surplus on revaluation of fixed assets .

Exercise : Prepare a Statement of Changes in Equity based on following data : Opening balance January 01, 2020: Opening balance January 01, 2020:

Share Capital Rs 500 000 , Revenue Reserves Rs 300 000 Capital Reserves Rs 400 000.

During the year following transactions took place:

- Profit for the year is Rs 700 000.
- Cash dividend declared and paid Rs 200 000 from revenue reserve
- Bonus Shares issued 30 % from Capital Reserves.

	Share cap	Revenue Reserves	Capital Reserves	Total EQUITY
Opening balance	500 000	300 000	400 000	1 200 000
Profit		700 000.		700 000
Cash dividend		-200 000		-200 000
Bonus shares	150 000		-150 000	0
	650 000	800 000	250 000	1 700 000