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Chapter 2

BRANCHES OF ACCOUNTING

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**AT THE END
OF THE
CHAPTER,
THE
STUDENTS
SHOULD BE
ABLE TO**

- 1. differentiate the branches of accounting;**
- 2. explain the kind or type of services rendered in each of these branches;**
- 3. make a list of businesses within the community on the types of accounting services they require; and**
- 4. solve exercises in the identification of the branches of accounting described through the types of services rendered.**

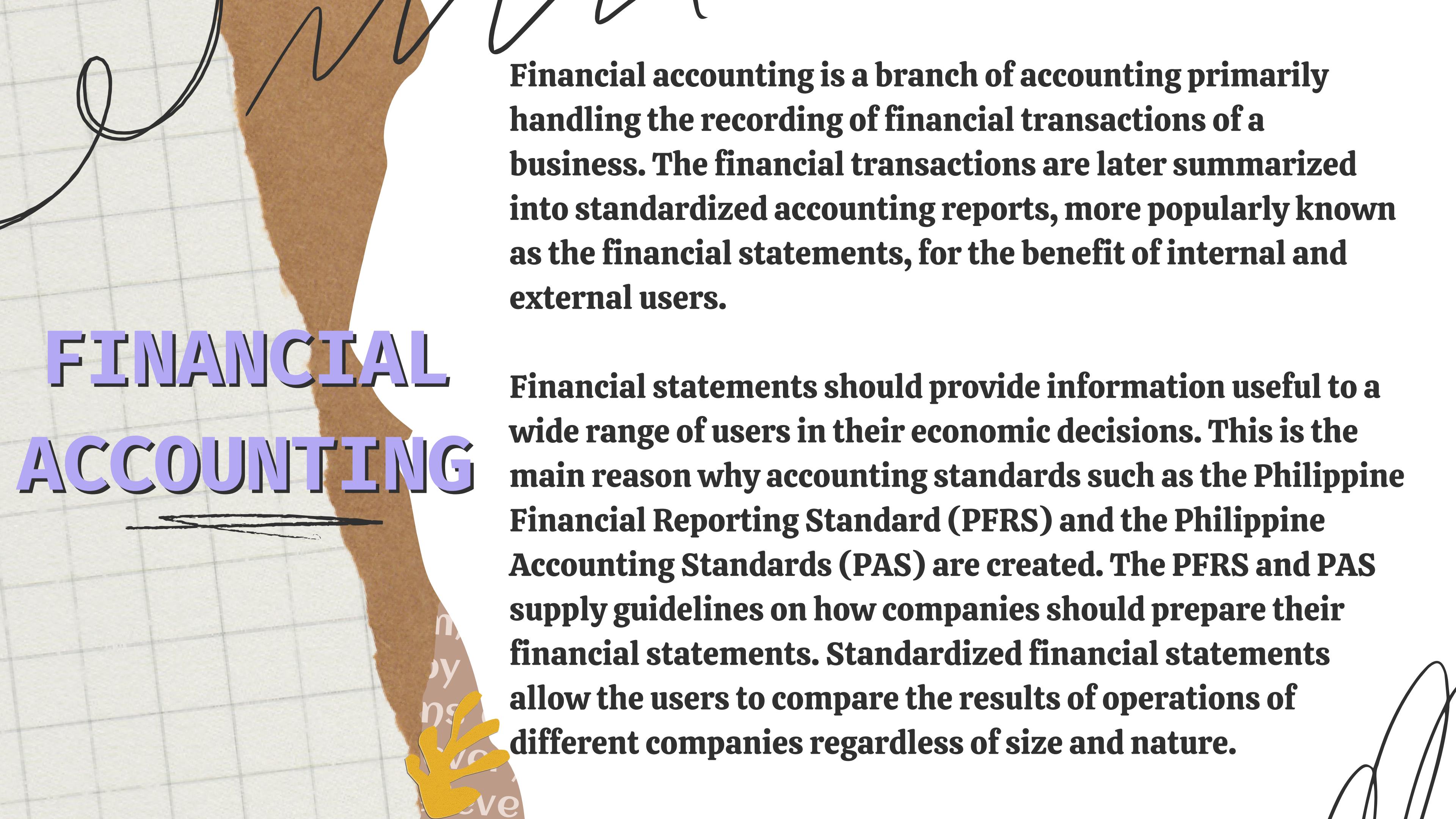
INTRODUCTION

Aside from the accounting process mentioned in Chapter 1 (i.e., identification - recording-communication), accountants can offer other services. In this chapter, we will tackle the different branches of accounting and the different services provided by these branches. There are eight branches of accounting as follows:

1. Financial accounting
2. Management accounting
3. Government accounting
4. Auditing
5. Tax accounting
6. Cost accounting
7. Accounting education
8. Accounting research

Each branch has its own functions and use.
We will discuss these branches one by one.





FINANCIAL ACCOUNTING

Financial accounting is a branch of accounting primarily handling the recording of financial transactions of a business. The financial transactions are later summarized into standardized accounting reports, more popularly known as the financial statements, for the benefit of internal and external users.

Financial statements should provide information useful to a wide range of users in their economic decisions. This is the main reason why accounting standards such as the Philippine Financial Reporting Standard (PFRS) and the Philippine Accounting Standards (PAS) are created. The PFRS and PAS supply guidelines on how companies should prepare their financial statements. Standardized financial statements allow the users to compare the results of operations of different companies regardless of size and nature.

GENERAL PURPOSE FINANCIAL STATEMENTS

Are the financial statements prepared to accommodate the information needs of persons who have no capability to request or acquire information directly from the company?

If the answer is yes, the financial statements are called general purpose financial statements. Otherwise, the financial statements are called special purpose financial statements.

GENERAL PURPOSE FINANCIAL STATEMENTS

Primary Users of General Purpose Financial Statements

- Investors
- Creditors
- Shareholders/Stockholders
- Government Agencies
- Auditors
- Other interested outside parties

Primary Users of Special Purpose Financial Statements

Top management (e.g. Board of directors of a company, CEO, CFO, COO)
Department managers (eg, sales manager, production manager)
Other internal parties

Predominantly, external parties use general purpose financial statements to evaluate the performance of the company. On the other hand, specific purpose financial statements are utilized by internal parties to guide them in the decision-making process for the company.

MANAGEMENT ACCOUNTING



Management accounting is a branch of accounting which focuses on the preparation of financial reports used by managers in their day-to-day decision-making. Reports generated using management accounting are for internal users only. As such, management reports need not follow accounting standards such as the PFRS and PAS. Additionally, unlike financial reports that are generated quarterly, semi-annually, or annually, management reports can be done daily, weekly, or whenever managers require a specific report. Management reports typically contain information regarding the amount of cash on hand, the level of sales revenue for a particular period, costs incurred, or even the comparison of actual results with budgeted amounts.

Aside from the frequency and the intended users of reports, management accounting differs from financial accounting in the nature of information produced. Financial accounting summarizes financial information gathered within a specified period. Thus, financial accounting provides information that is historical. Meanwhile, management accounting information is forward-looking. It contains forecasted information used by managers in planning.

ROLES OF MANAGEMENT ACCOUNTANTS

According to the Chartered Institute of Management Accountants (CIMA), chartered management accountants perform the following roles:

- Advise managers about the financial implications of projects
- Explain the financial consequences of business decisions
- Formulate business strategy
- Monitor spending and financial control
- Conduct internal business audits
- Explain the impact of the competitive landscape
- Bring a high level of professionalism and integrity to the business

It is emphasized that management accounting is used in deciding how the business should act going forward. The use of management accounting provides value to the business since it assists the company in selecting only those activities that deliver benefits.

MANAGEMENT ACCOUNTING SKILL SET

In addition to strong accounting fundamentals, management accountants should also possess the following strategic business and management skills:

- **Analysis.** Management accountants should be able to analyze information and use it to make business decisions.
- **Strategy.** Management accountants should be able to formulate business strategies that will increase the company's wealth and create value for the company's shareholders.
- **Risk Management** accountants should be able to identify risks that can potentially have detrimental effects to the company. At the same time, management accountants should give recommendations on how to manage such risks.
- **Planning.** Management accountants should be able to apply accounting techniques in the planning and budget creation phase of a business.
- **Communication.** Management accountants should be able to identify what information the management needs and also explain the numbers to non-financial managers.

ETHICAL CODE

Even though management reports do not follow the requirements imposed by accounting standards like the PFRS and PAS, management accountants are still expected to follow the CIMA code of ethics.

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GOVERNMENT ACCOUNTING

According to Section 109 of Presidential Decree 1445, government accounting is defined as an accounting system which "encompasses the process of analyzing, recording, classifying, summarizing, and communicating all transactions involving the receipt and disposition of government fund and property and interpreting the result thereof."

Section 110 of the same decree lays down the objectives of government accounting:

- 1. To provide information concerning past operations and present conditions**
- 2. To provide a basis for guidance for future operations**
- 3. To provide for control of the acts of public bodies and offices in the receipt, disposition and utilization of funds and property.**
- 4. To report on the financial position and the results of operations of government agencies for the information and guidance of all persons concerned.**

NEW GOVERNMENT ACCOUNTING SYSTEM (NGAS)

As citizens of the Philippines, we are very much concerned on the stewardship of the government of public resources. We do not want the country's funds to be used for personal reasons by erring public officials. Instead, we want these funds to be used for public projects that will benefit many constituents.

One of the main features of the NGAS is that it enhances responsibility accounting in all agencies. Simply stated, responsibility accounting relates financial results to a particular responsibility center (i.e., agency). If there is a problem with the handling of funds by the DPWH, for example, people in that agency will be the ones accountable. This system of placing accountability in each agency discourages misappropriation and misuse of public funds.

GOVERNMENT ACCOUNTING PROCESS

Government accounting starts after the declaration of the General Appropriations Act (GAA). The GAA is the enacted budget of the country for the upcoming year. The GAA has the force of law and it states how much an agency can spend for the year. If it is indicated that P500M is available for the DPWH to implement its projects, the agency cannot spend more than this amount.

The government accounting process involves the Commission on Audit (COA), the Department of Budget and Management (DBM), the Bureau of Treasury (BTr), and all other government agencies.

The COA is responsible for the keeping of the government's general accounts. Think of our government as one big, non-profit organization. The COA is tasked to keep and update the accounting books of the whole organization. Moreover, the COA disseminates accounting rules and regulations to be used by all agencies.

AUDITING

Financial statements prepared by a company are often the only source of information an interested outside party has regarding the results of the company's operations. Information included in the financial statements greatly influences the decisions made by the users. Because of this, there seems to be a conflict of interest between the users and the source of the financial statements.

The users of the financial statements want information about the company that is truthful, reliable, and relevant. In making their economic decisions, users want to use information that depicts the current condition of the company. On the other hand, management (or any other party preparing the financial statements) usually wants to present information indicating good results. Some managers will even falsify or manipulate the records of financial transactions just to show decent results. This is exactly what happened in Enron as featured in our featured story.

TAX ACCOUNTING

Taxes are the lifeblood of the government. Without the taxes the citizens pay, the government cannot perform its functions. Thus, it is imperative that the collection of taxes be unhindered. The recording of financial transactions mentioned in Chapter 1 follows specific guidelines provided by the PFRS and PAS. Tax accounting records some financial transactions in a different manner. It adheres to some guidelines in the PFRS and PAS, but it is not required to implement everything written in such standards. Tax accounting follows the pronouncements of the National Internal Revenue Code (NIRC).

The NIRC is to tax accounting as the PFRS and PAS are to financial accounting. To illustrate the difference, let us look at a particular example. Starbucks offers its customers a card that you can use to pay for your orders. The process is simple. You ask the cashier to load the card; you pay for the amount of load; and then your card will reflect the balance available for you to use. You can use the card for future transactions with Starbucks Under the PFRS and PAS, Starbucks will not recognize the amount you paid as revenue until you use the balance in your card in the future. Under the NIRC, Starbucks recognizes the revenue when the company received the payment from you. Thus, if Starbucks recognizes the revenue, it is taxable.

COST ACCOUNTING

Cost accounting is a branch of accounting that provides information for management accounting and financial accounting (Horngren et al. 2011). For example, cost accounting helps measure the cost of a bicycle for a bicycle-selling company. This information supports management in deciding how many bicycles to produce, the selling price of the bicycle, or valuing the inventory of bicycles in the company's financial statements.

TERMS USED IN COST ACCOUNTING

These are just some of the terms used in cost accounting. For the purposes of this book, you only need to understand these basic cost concepts. The application of cost accounting is not within the scope of this book.

- **Cost** - the resource sacrificed to achieve an objective (e.g., money, resources time, etc.)
- **Cost object** - anything that you wish to find the cost of (e.g., cost of a pair of jeans cost of a pair of Jordan XI shoes)
- **Cost driver**-an activity that is a cause of the incurrence of costs (e.g., the number of working hours is related to the amount of salaries a company pays)

ACCOUNTING EDUCATION

The Bachelor of Science in Accountancy (BSA) in the Philippines is normally a 5-year program composed of subjects in accounting, audit, administration, and business laws and taxation. Although the subjects usually highlight the business environment, the scope of the topics in BSA also covers other fields such as banking and finance, government, non- profit organizations, and the academe. Students of the course are also trained to create and understand computerized accounting systems to cope with the rapidly changing technology.

Most schools use a combination of diverse teaching techniques to explain accountancy to students. Some of these methods are classroom discussions, case analysis, individual and group reporting, feasibility studies, and lectures from renowned individuals in the field. Other schools require students to undergo an internship program equivalent to one subject. This is to enable the students to have a feel of the application of accounting in real life.

ADMISSION REQUIREMENTS FOR BSA

According to the Commission on Higher Education (CHED), the standards of admission to any BSA program should be sufficiently rigorous and demanding. Only universities which can demonstrate the capability to teach accountancy in a sufficiently high level are allowed to do so.

Requirements at each school are different, but the common requirements include:

- Must be a high school graduate
- Must have a college entrance examination of above average or depending on the specific rating set by the school
- Aside from the college entrance examination, must pass the separate aptitude test specific for BS in Accountancy
- Must pass the interview conducted by the college admission officer
- Some schools require a high school QPA of 85% and above with no grade less than 80% in all subjects.
- There are schools who require students to have an 85% or higher average rating in the National Secondary Assessment Test (NSAT). As set by CHED, all schools must conduct an English Proficiency examination to all BS in Accountancy applicants.
- Admission for Philippine Educational Placement Test (PEPT) passers mainly depends on the school's discretion since some colleges and universities offer only selected courses.

BOARD EXAM

Before a BSA graduate can practice accountancy, he/she needs to pass the Certified Public Accountant Licensure Examination. The CPA Licensure Exam is a comprehensive test composed of seven subjects. Each subject will be taken within 3 hours so the exam will be for 21 hours all in all. A candidate should achieve a general average of at least 75% with no rating below 60% in any of the seven subjects in order to pass the exam.

ACCOUNTING RESEARCH

Accounting research, as the name suggests, is a branch of accounting that deals with the creation of new knowledge. Combining the models produced by the hard sciences in research and testing with financial statements, stock prices, surveys, and experiments, we can gain a specific perspective and basis on the following:

- Deciding and implementing new accounting and auditing standards
- Presenting unusual economic transactions in the financial statements
- Learning how new tax laws impact clients and employers
- Discerning how the accounting profession affects the capital markets through academic accounting research.

Researchers in the accounting field also apply the scientific method like their counterparts in the sciences. With the constantly evolving field of accountancy, it is expected that accounting research will continue to play a vital role in the future.

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