What is Accounting

Accounting is the art of recording, classifying and summarising in a significant manner and in terms of money, transactions and events which are in part at least, of a financial character, and interpreting the result thereof.

Note: Accounting is simply an art of record keeping.

Procedure of Accounting

- Generating financial Information
  - Recording
  - Classifying
  - Summarising
- Using the financial Information
  - Analysing
  - Interpreting
  - Communicating

Transaction: A business, performance of an act an agreement

Event: A Happening, as a consequence of transaction(s), a result

Nature and scope.

Recording: It is the process of entering the transaction and events in the books called 'Journal' in the chronological manner

Classifying: It is the process of posting of entries in the ledger so that transaction of similar type are accumulated at one place.

Summarizing: It is concerned with the preparation of financial statement such as Income statement (P&L account), Balance sheet, and Cash flow statement.

Analyzing: It is concerned with the establishment of relationship between the various item or group of items taken from P&L acc. or Balance sheet or both. Its purpose is to identify the financial strengths and weakness of the enterprise. It provides the basis for interpretation.

Interpreting: Interpreting is the last stage of accounting process. It is concerned with explaining the meaning and significance of the relationship established by the analysis. In fact, interpretation is the main function of accountant in the present condition since the routine work of recording, classifying and summarizing business transaction can be easily handled by the electronic devices like computer.

Communicating: It is concerned with the transmission of summarized, analyzed and interpreted information to the users to enable them to make reasoned decisions.

Advantages and Disadvantages

Functions - advantages

1) Measurements

Accounting measures past performance of the business entity and depicts its current financial position.

2) Forecasting

Accounting helps in forecasting future performance and financial position of the enterprise using past data.

3) Decision Making

Accounting provides relevant information to the users of accounts to aid rational decision-making.

4) Comparison & Evaluation

Accounting assesses performance

achieved in relation to targets and discloses information regarding accounting policies and contigent liabilities which play an important role in predicting comparing and evaluating the financial results.

5) Control
Accounting also identifies weakness of the operational system and provides feedbacks regarding effectiveness of measures adopted to check such weakness.

Limitations - disadvantages

1) The factors which may be relevant in assessing the worth of the enterprise don't find place in the accounts as they cannot be measured in terms of money eg goodwill loyalty and the skill of the personnel etc.

2) Accounting ignores changes in some money factors like inflation etc.

3) There are occasions when accounting principles conflict with each other.

4) Balance sheet reflects the position of the enterprise on the day of it's preparation and not on the future date while most of the users are interested in having knowledge about the future of the enterprise.

5) Sometimes accounting estimates depends on the personal judgement of the accountant which may result in inaccurate results.

Accounting Concepts
Accounting concepts defines the assumptions on the basis of which financial statements of a business entity are prepared. Certain concepts are perceived, assumed and accepted in accounting to provide a unifying structure and internal logic to accounting process.

Accounting Principles
Accounting Principles are simply body of doctrines and assumptions on the basis of which financial statements are prepared.

Accounting principles must satisfy the following conditions

- They should be based on real assumptions
- They must be simple, understandable and explanatory
- They must be followed consistently
- They should be able to reflect future predictions
- They should be informational for the users

Accounting Conventions
Accounting conventions emerge out of accounting practices, commonly known as accounting principles adopted by various organization over a period of time

→ Money measurement concepts
As per this concept only those transactions which can be measured in terms of money are recorded. Transactions and events that cannot be expressed in terms of money are not recorded in the business books.

→ accrual concept
The effects of transactions and other events are recognised on mercantile basis i.e when they occur and they are recorded in the accounting records and reported in the financial statements of the periods to which they relate.

→ conservation
conservatism states the accountant should not anticipate income and should provide all possible losses. when there are many alternative values of an asset, an accountant should choose the method which leads to the lesser values.

→ consistency
accounting policies are followed consistently from one period to another to achieve comparability of the financial statements of an enterprise through time.

→ materiality
It permits other concepts to be ignored, if the effect is not considered material.

Accounting Terminology

1) Assets
Tangible objects or intangible rights owned by an enterprise and carrying probable future benefits.

2) Liability
The financial obligation of an enterprise other than owner's funds.

3) Expense
A cost relating to the operations of an accounting period or the revenue earned during the period or the benefits of which do not extend beyond that period.

4) Expenditure
Incurring a liability, disbursement of cash or transfer of property for the purpose of obtaining assets, goods or services

5) Capital
Generally refers to the amount invested in an enterprise by its owners

6) Goodwill
An intangible asset ~~during~~ arising from business connections or trade name or reputation of an enterprise.

7) Sundry Creditors
Amount owned by an enterprise on account of goods purchased or services received or in respect of contractual obligations

8) Sundry Debtors
Persons from whom amounts are due for goods sold or services rendered or in respect of contractual Obligations.

9) Gain
A monetary benefit, profit or advantage resulting from a transaction or group of transactions.

10) Profit
A general term for the excess of revenue over related cost.

Accounts

- Personal Accounts
  - Natural
  - Artifical
  - Representative
- Impersonal Accounts
  - Real accounts
  - Nominal accounts

Personal Account
Debit the receiver
Credit the giver

Real Account
Debit what comes in
Credit what goes out

Nominal Accounts
Debit are all expenses and loses
Credit are all income and gains

American Rule

Asset + → Dr
Asset − → Cr

Liability + → Cr
Liability − → Dr

Expense (−), Income (+) → Cr
Expense (+), Income (−) → Dr