FINANCIAL ACCOUNTING AND MANAGEMENT

UNIT 1: INTRODUCTION TO ACCOUNTING

BOOK KEEPING

It is the art of recording the business transactions in a set of books systematically.

The two systems in book-keeping are

1. Single entry system of book-keeping and

2. Double entry system of book-keeping

The set of books are

1. Journal

2. Subsidiary books

3. Ledger

4. Trial Balance and

5. Final Accounts.

ACCOUNTING

Accounting may be defined as the art of recording, classifying and consolidating business transactions that are financial in nature for audit and tax purposes.

ACCOUNTANCY

Accountancy is the theory and principles of accounting.

OBJECTIVES OF ACCOUNTING

1. To provide information about the business activities to the owners, stake holders or investors and creditors facilitating them to take decisions on investment and lending.

2. To effectively manage the material resources available.

3. To facilitate social functions and control.

4. To provide information regarding accounting policies.

ACCOUNTING CONCEPTS

1. Business entity concept

The transactions of a business are to be kept separate from those of its owners. By doing so, there is no intermingling of personal and business transactions in a company's financial statements.

2. Going concern concept

Financial statements are prepared on the assumption that the business will remain in operation in future periods.

3. Consistency concept

Once a business chooses to use a specific accounting method, it should continue using it on a go-forward basis. By doing so, the financial statements prepared in multiple periods can be reliably compared.

4. Money Measurement Concept

Business transactions can only be recorded in terms of their monetary value.

5. Conservatism concept

Revenues are only recognized when there is a reasonable certainty that they will be realized, whereas expenses are recognized sooner, when there is a reasonable possibility that they will be incurred. This concept tends to result in more conservative financial statements.

6. Dual Aspect Concept

Each transaction has two aspects. When a business acquires an asset, it has to pay money. Acquiring an asset and paying money are two sides of the coin. Similarly, if the asset is acquired through credit, there arises a liability to that extent. Thus if there is an increase in asset, there will be increase in liability also.

Capital = Assets-Liabilities

7. Cost Concept

The transactions are recorded keeping in mind the actual cost involved and this concept does not consider the projected value or appreciation.

8. Matching concept

The expenses related to revenue should be recognized in the same period in which the revenue was recognized. By doing this, there is no deferral of expense recognition into later reporting periods, so that someone viewing a company's financial statements can be assured that all aspects of a transaction have been recorded at the same time.

ACCOUNTING CONVENTIONS

1. Convention of Disclosure

This convention requires that accounting statements should be honestly prepared and all significant information should be disclosed therein. That is, while making accountancy records, care should be taken to disclose all material information. Here the emphasis is only on material information and not on immaterial information.

2. Convention of Consistency

Rules and practices of accounting should be continuously observed and applied. In order to enable the management to draw conclusions about the operation of a company over a number of years, it is essential that the practices and methods of accounting remain unchanged from one period to another.

3. Conservatism

According to this convention, accounts follow the rule "anticipate no profit but provide for all possible losses", while recording business transactions.

4. Materiality

The term materiality refers to the relative importance of an item or an event. An item is "material" if knowledge of the item might reasonably influence the decisions of users of financial statements. Accountants must be sure that all material items are properly reported in the financial statement.

BRANCHES OF ACCOUNTING

1. Financial Accounting

The main purpose is to record the business transactions in the books of accounts enabling businessmen to know the results. In general, the term accounting refers to financial accounting only.

2. Cost Accounting

Cost accounting is the process of recording, classifying, analyzing, summarizing, and allocating costs associated with a process, and then developing various courses of action to control the costs.

3. Management Accounting

Both financial and cost accounting methods and results contribute to management accounting where the data is interpreted mainly for arriving at optimal managerial decisions.

ACCOUNTING TERMS

CAPITAL: Capital refers to investment made by owners of a business enterprise in the form of cash or kind.

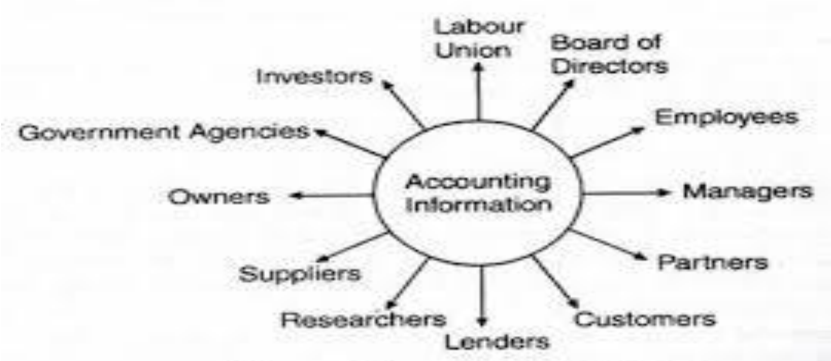
DRAWINGS: Drawings refers the money or any other item used or withdrawn by owners for personal purposes.

GOODS: Goods refers to articles, commodities, things with which business deals. Example: stationery, books pens, pencils, table, cupboards.

PURCHASES: Purchase refers to goods purchased by the business.

PURCHASE RETURNS: When goods purchased are returned to the supplier of goods on account of damage or defect.

USERS OF ACCOUNTING INFORMATION



Users of Accounting Information

Examples of internal users are owners, managers, and employees.

External users are people outside the business entity (organization) who use accounting information. Examples of external users are suppliers, banks, customers, investors, potential investors, and tax authorities.

ADVANTAGES OF ACCOUNTING

1. Maintenance of business records-

Accounting helps to maintain the business records in a systematic manner.

2. Preparation of financial Statements-

It helps in the preparation of financial statements.

3. Useful in comparing the results-

Accounting information is also used to compare the result of current year with the previous year to analyze the changes.

4. Decision Making-

It helps the managers in the decision making process.

5. Information to users-

It provides information to other interested parties such as shareholders, creditors, investors, customers, government, employees, regulatory bodies etc.

6. Information to Concerned Authorities-

It provides information to authorities like Income Tax Department etc

7. Source of Evidence

Accounting information can be produced as evidence in the legal matter.

8. It helps in valuation of business.

DISADVANTAGES OF ACCOUNTING

1. Monetary transactions are recorded

The items expressed in monetary terms are recorded in the accountings where as the items which are nonmonetary nature not recorded.

2. Based on estimates

Sometimes accounting data are recorded on the basis of estimates and which could be inaccurate.

3. Recorded at Cost Price

Fixed assets are recorded as the original cost.

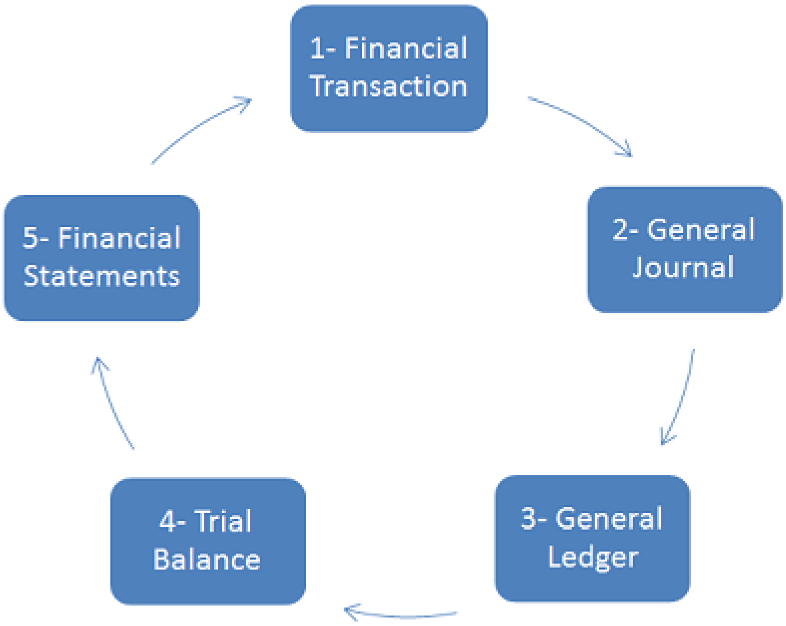
4. Doesn’t show true financial statements

Value of money does not remain stable so accounting value does not show true financial results.

5. Manipulation

Accounting can be manipulated and biased

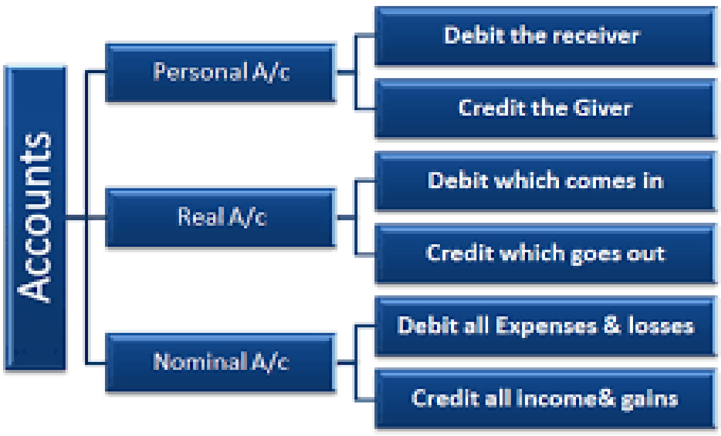
ACCOUNTING CYCLE



ACCOUNTING PRINCIPLES

Accounting principles are the rules and guidelines that companies must follow when reporting financial data.

RULES OF ACCOUNTING



ACCOUNTING STANDARDS

An accounting standard is a common set of principles, standards and procedures that define the basis of financial accounting policies and practices.

List of Indian Accounting Standards

Ind AS No.	Name of Indian Accounting Standard
Ind AS 101	First-time adoption of Ind AS
Ind AS 102	Share Based payments
Ind AS 103	Business Combination
Ind AS 104	Insurance Contracts

Ind AS 105	Non-Current Assets Held for Sale and Discontinued Operations
Ind AS 106	Exploration for and Evaluation of Mineral Resources
Ind AS 107	Financial Instruments: Disclosures
Ind AS 108	Operating Segments
Ind AS 109	Financial Instruments
Ind AS 110	Consolidated Financial Statements
Ind AS 111	Joint Arrangements
Ind AS 112	Disclosure of Interests in Other Entities
Ind AS 113	Fair Value Measurement
Ind AS 114	Regulatory Deferral Accounts
Ind AS 115	Revenue from Contracts with Customers
Ind AS 1	Presentation of Financial Statements
Ind AS 2	Inventories Accounting
Ind AS 7 & in only AS 3	Statement of Cash Flows
Ind AS 8	Accounting Policies, Changes in Accounting Estimates and Errors
Ind AS 10	Events after Reporting Period
Ind AS 11	Construction Contracts
Ind AS 12	Income Taxes
Ind AS 16	Property, Plant and Equipment
Ind AS 17	Leases
Ind AS 18	Revenue
Ind AS 19	Employee Benefits
Ind AS 20	Accounting for Government Grants and Disclosure of Government Assistance
Ind AS 21	The Effects of Changes in Foreign Exchange Rates
Ind AS 23	Borrowing Costs
Ind AS 24	Related Party Disclosures
Ind AS 27	Separate Financial Statements
Ind AS 28	Investments in Associates and Joint Ventures
Ind AS 29	Financial Reporting in Hyper inflationary Economies
Ind AS 32	Financial Instruments: Presentation
Ind AS 33	Earnings per Share
Ind AS 34	Interim Financial Reporting
Ind AS 36	Impairment of Assets
Ind AS 37	Provisions, Contingent Liabilities and Contingent Assets
Ind AS 38	Intangible Assets
Ind AS 40	Investment Property
Ind AS 41	Agriculture

ADVANTAGES / IMPORTANCE OF ACCOUNTING STANDARDS

1. Accounting standards help investors in judging for company.

2. Accounting standards helps the chartered accountants to deal with their clients by providing rules and regulations

3. Accounting standards helps in reporting financial statements

4. Accounting standards helps the tax authorities and government officials.

5. Accounting standards helps in reliable documents for the purpose of analysis and interpretation of data

FINANCIAL STATEMENTS OF A BUSINESS

For BCA – 1^{ST} Year

MEANING OF FINANCIAL STATEMENTS

Financial Statements are the end products of accounting process. They provide information about the profitability and the financial position of a business. A set of financial statements include –

- **PROFIT AND LOSS ACCOUNT (STATEMENT OF PROFIT AND LOSS) :** It shows the financial performance i.e, the result of business operations during an accounting period. It is also known as income statement.

- **BALANCE SHEET:** It is a statement of Assets and Liabilities, i.e, the financial position of an enterprise at a given date.

- **CASH FLOW STATEMENT:** It is a Statement of Cash Inflows and Cash Outflows of a business.

OBJECTIVES OF PREPARING FINANCIAL STATEMENTS:

- To present a True and Fair View of the financial performance (i.e Profit / Loss) of the Business.

- To Present a True and Fair View of the Financial Position (i.e Assets/ Equities and Liabilities) of the business.

TRADING & PROFIT AND LOSS ACCOUNT:

- Trading & Profit and Loss Account is prepared to determine the profit earned or loss incurred by the business enterprise during the accounting period.

- It is basically a summary of Revenue and Expenses of the business and calculates the net figure termed as profit or loss.

- Trading & Profit and Loss Account summarizes the performance for an accounting period.

- It is prepared by transferring the balances of revenues and expenses to the trading and profit and loss account from the trail balance.

- Trading and Profit and loss Account is also an account with debit and credit side.

ITEMS IN THE PROFIT AND LOSS ACCOUNT

ITEMS ON DEBIT SIDE – Inclusive List

Opening Stock

DIRECT EXPENSES:

- Purchases
- Purchase Returns
- Wages
- Carriage Inwards / Freight Inwards

INDIRECT EXPENSES:

- Fuel / Water /Power / Gas Expenses
- Packaging Materials and Packing Charges
- Salaries
- Rent
- Interest Charges
- Commission
- Repairs and Maintenance
- Miscellaneous Expenses

ITEMS IN THE PROFIT AND LOSS ACCOUNT

ITEMS ON CREDIT SIDE – Inclusive List

- Sales
- Sales Returns
- Closing Stock
- Other Incomes

TRADING & PROFIT AND LOSS ACCOUNT - FORMAT

TRADING AND PROFIT AND LOSS ACCOUNT OF ABC

For the Year ending March-31st-2017

Dr Cr

Expenses /Losses	Amount (Rs)	Revenues /Gains	Amount (Rs)
Opening Stock	....	Sales	....
Purchases	....	Less: Sales Returns	
Less: Purchase Returns	....	Closing Stock	
Wages	....		
Carriage Inwards /Freight Inwards / Cartage	....		
Gross Profit /Loss	....		
TOTAL	xxxxx	TOTAL	xxxxx
Rent	......	Gross Profit/ Loss	....
Salaries	......	Interest Received	....
Fuel / Gas	....		
Electricity Charges	....		
Commission	......		
Discount Allowed	....		
Repairs and Maintenances / Renewals	....		
Advertisement and Marketing Expenses	....		
Audit Fees	....		
Bad Debts	......		
Net Profit/Loss (Transferred to capital A/c)	....		
TOTAL	xxxxx	TOTAL	xxxxx

Trading Account

Profit & Loss Account

EQUATION FORM OF THE PROFIT AND LOSS ACCOUNT

- GROSS PROFIT = SALES – (PURCHASES+DIRECT EXPENSES)

  COST OF GOODS SOLD = PURCHASES + DIRECT EXPENSES (if no closing stock)

  COST OF GOODS SOLD = PURCHASES + DIRECT EXPENSES – CLOSING STOCK (if closing stock exists)

- NET PROFIT = GROSS PROFIT – INDIRECT EXPENSES

BALANCE SHEET

- The Balance Sheet is a statement prepared for showing the financial position of the business.
- Balance Sheet summarizes its assets and liabilities at a given date.
- The Assets reflects on the right side of the Balance Sheet and liabilities (including capital) reflects on the left side the of the Balance Sheet.
- It is prepared at the end of the accounting period.
- It is called Balance Sheet because , it is a statement of balances of ledger accounts that have not been transferred to trading and Profit and Loss Account and are to be carried forward to the next year.

RELEVENT ITEMS IN THE BALANCE SHEET (Few Items)

- Capital
- Long Term Liabilities
- Short Term Liabilites
- Fixed Assets
- Intangible Assets
- Investments
- Current Assets

BALANCE SHEET - FORMAT

BALANCE SHEET OF ABC

As at March-31st 2017

LIABILITIES	AMOUNT (RS)	ASSETS	AMOUNT (RS)
CAPITAL (OWNERS FUND)	....	FIXED ASSETS (NON	....
Add : Profits /Loss		CURRENT ASSETS)	....
		Land	....
LONG TERM LIABILITES (NON CURRENT	......	Building	....
LIABILITES):		Furniture	
Long Term Loans		Good Will	
	....	Investments (Long Term)	
CURRENT LIABILITES :	....		......
Short Term Loans	....	CURRENT ASSETS:	......
Sundry Creditors	....	Sundry Debtors	....
Bills Payable		Cash Balances	....
Bank Over Draft		Bank Balances	
		Closing Stock	
	Xxxxxxx		xxxxxxxx