**Meaning and selection of accounting policies**

Accounting principles are the specific principles, conventions, rules, and practices that an entity applies in preparing account's statements. Whereas accounting policies are rules to which a company adheres and follows. Selection of accounting policies is a major goal for a company to establish. For various purposes like transactions, sales management etc. selection of accounting policies is necessary. Accounting policies are specific policies which alter at times to help in maintaining the profit rate. Therefore, the selection of accounting policies changes with a change in the requirements of the company.

**Overview**

A company follows certain rules and regulation in every decision it makes. Accounting policies form the base of those decisions. Specific policies are very important. A company's accounting policies display its management records whether it is progressive or aggressive.



Likewise, a firm develops a pattern to feed the basic fundamental of marketing i.e. earning profits. Accounting is done to keep a record of progress graph and the policies support the graph to rise.

**Meaning of Accounting Policies**

The accounting policies include methods, procedures and measuring systems to present information in financial statements. A company prepares a quarterly earnings report to report their performance. The report includes earnings per share, earnings from daily activities, net sales, and net income. The company demonstrates this report to investors. Based on the quarterly earnings report, investors process the accounting information and then decide if they want to invest in the company.

**Selection of Accounting policies**

Companies work on certain key points for selecting accounting policies. Companies choose the following considerations as a basis of these policies.

* **Precise and Accurate Presentation**

Accounting policies should clearly convey the account's information. Rather than making unnecessary adjustments, the policies must present every piece of information as genuine and simple. For example, a company owns resources are assets. At first, assets add to the expense list. Afterward, its future potential is measured.

Applying the accuracy criterion, the firm would make an inventory list. It would include expenses used on the asset during a period and the services consumed during the period. There is only one associated limitation. A firm can't precisely measure an asset's usability and the remaining potential it holds.

* **Conservatism**

In choosing among generally accepted principles, a firm's priority goes to policies that have conservative measures of net income. As business offers many uncertainties, a conservative approach towards benefits is always preferable.

Accordingly, Conservatism implies that policies form a major part of accounting. They must recognize expenses as fast as possible. In addition, they must delay revenues as long as applicable. This method minimizes cumulative reported earnings.

* **Profit Maximization**

Working in opposite direction to Conservatism, this technique supports maximizing cumulative reported earnings. That is, policies must recognize revenues as quickly as possible. And to delay expenses as long as possible. Use of this accounting process is that a firm generates profits. The report should be a favorable one. It must showcase a firm's growth.

* **Income Smoothing**

Another criterion for selecting accounting policies is Income Smoothing. As the name suggests, income smoothing works to make the flow of income easy. It suggests to first analyze the earnings. Then, minimize fluctuations in earnings. This will decrease risks linked with invested shares. In return, chances of earnings will increase.

This criterion also suggests net income, revenues and expenses to be smoothed. So, basically, this policy works on taking shorter steps leading to an ultimate goal i.e. raising profits.

**Restrictions on Selecting Accounting Principles**

There are a number of policies for a business to try and adapt. This does not necessarily mean that a firm can choose a policy whenever it likes. Also, it cannot discard a policy when it doesn't suit the business anymore. It has to obey certain rules. Generally, a firm compiles a set of policies and as a permanent set. Whereas, a secondary set is prepared to cover other requirements.

Even if a company separates financial reports and income tax reports, the practices are legal. The government organization just wants report related to a firm clear and understandable. The reports must be open to examination. Financial statements should disclose the firm's owned assets. It should not hide any previous dues that may harm in future.

**Conclusion**

Accounting policies are strict rules and a company must follow them. After all, these policies benefit everyone including the firm. If you buy shares from a trusted firm and it vanishes from the view in days, how would you feel? Similarly, if you are investing in a business, make sure you are giving your best to receive the best. Accounting policies help to give a true meaning to a business. Therefore, to maintain the decorum of business standards, apply necessary policies in your business. Also, make them open to concerned authorities. This will help your business grow.

**Solved Questions For You**

**Question:** What is the importance of Accounting policies disclosure?

**Answer:** Suppose, government authorities find a mismatch in the accounting policies you present vs the policies you show. This scenario might end up in the cancellation of your business licence. Because authorities will consider any practice illegal if the firm skips mentioning that policy. Without any further notice, it reserves the right to cancel your licence. Therefore, it is better to disclose Accounting Policies immediately after finalising policies.

**Question:** What is meant by Generally Accepted Accounting Principles (GAAP)?

**Answer:** Generally Accepted Accounting Principles (GAAP) are a basic set of accounting principles commonly available. Companies follow the same protocol as a standard to clarify their accounting-related doubts. It is a necessary document that companies must follow when they compile their financial statements.