

CH.1 INTRODUCTION TO ACCOUNTING

Meaning of accounting

Accounting is the measurement, processing and communication of financial information about business and corporation. Accounting has several subject areas including financial accounting, management accounting, auditing and taxation etc. It gives information about

- Resources available (assets and liabilities)
- How the resources have been utilized (efficiently)
- The results achieved by their use (profit and loss)

Definition

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

(By american institute of certified public accounts)

Features / characteristics of accounting

1. **Identifying financial transaction:** by their bills, receipt and evidence of transaction.
2. **Measuring the identified transaction:** in terms of money.
3. **Recording:** it is the process of recording transaction in journal.
4. **Classifying:** it is the process of collecting similar transaction at one place, by opening a/c in ledger book.

5. **Summarising:** it means presenting the collected data in a manner which is understandable and useful to internal as well as external user of business. Ex: trial balance , financial statements.
6. **Analyses and interpretation:** it is the process of reviewing and analyzing a company's financial statement to make better economic decisions. It is used by variety of stakeholders, such as creditors, public , government, equity investors.
7. **Communicating:** accounting information should be provided in time to user so that the decisions are taken at appropriate time.

BOOK KEEPING

It is the process of recording financial transaction in books of accounts. It involves :-

- ★ Identification
- ★ Measuring
- ★ Recording
- ★ Classification

It is a part of accounting and narrower term than accounting.

OBJECTIVES OF ACCOUNTING:

- ★ Record of financial transaction.
- ★ Determine profit&loss (trading and p&l a/c)
- ★ Determine financial position (balance sheet)
- ★ Helps in management
- ★ Communicating accounting information to users
- ★ Protecting business assets

FUNCTIONS OF ACCOUNTING:

- ★ Maintaining systematic accounting records (principal, concept)
- ★ Preparation of financial statement(p&l,balance sheet)
- ★ Meeting legal requirements(companies act,income tax act)
- ★ Communicating information to users(external & internal)
- ★ Assistance to management(decision making)

LIMITATIONS OF ACCOUNTING:

- ★ It is not fully exact(based on estimation)
- ★ It does not indicates realisable value
- ★ Ignores qualitative elements(public relation,quality of staff)
- ★ Ignores effect of price level changes
- ★ It may lead to window dressing.

USERS OF ACCOUNTING INFORMATION:

1. INTERNAL USERS
2. EXTERNAL USERS

1. INTERNAL USERS: THESE ARE THE USERS WHO ARE ENGAGED IN DAY TO DAY ACTIVITIES OF ORGANISATION.THE USERS ARE AS FOLLOWS:

- Owners (about profit&doss)
- Management(decision making)
- Employees (about bonus)

EXTERNAL USERS: outsiders not engaged in internal management and activities.external users are as follows:

- Banks and financial institutions (safety and recovery of loan)
- Investors and potential investors(know about earning capacity)
- Creditors(for credit-worthiness)
- Government(for tax)

- Researchers
- Consumers(cost of production)
- Public(employment)

QUALITATIVE CHARACTERISTICS OF ACCOUNTING INFORMATION:

1. Reliability(verifiable)
2. Relevance(relevant to users)
3. Understandability
4. Comparability