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VIRTUAL COACHING CLASSES
ORGANISED BY BOS, ICAI

FOUNDATION LEVEL
PAPER 1: PRINCIPLES AND PRATICE OF ACCOUNTING

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CHAPTER 1- THEORETICAL FRAMEWORK

- There are 9 units in total for this chapter
- This chapter mainly deals with the theory part and introduction to the accountancy subject.
- What is Accounting- purpose and methodology, branches in accounting- the principles/conventions/concepts, the distinction between capital and revenue transactions, the Accounting standards and Ind AS.
- All of the above which form an initial base for understanding the concept in depth have been combined together to understand the entire concept in brief.
- Examination point of approach- Each chapter will have discussion of the past examination question papers at the end along with the MCQ's.

Unit 2-Accounting concepts, principles and conventions

- Generally the concept of having the accounting principles, conventions and assumptions is to eliminate the disparities that can be caused during the preparation of the financial statements.
- To avoid any such gross misstatements- while recording itself- it has been brought out that there are certain principles/concepts/conventions to be followed so that the application and recording of the transactions does not cause much disparity in the preparation of the financial statements.
- Accounting concepts refers to any idea or notion which has universal application. These concepts have been developed over a period of time to provide unifying structure and logic to accounting process. They are the assumptions based on which principles are developed. For ex- Going concern, consistency and Accrual
- Accounting principles are body of doctrines- basically set of rules to be used where in there are more than one convention applicable- For ex- depreciation- which depreciation method will be used is decided based on the principles- like it must depict the real business set up, it should be simple, understandable and explanatory.

Unit 2-Accounting concepts, principles and conventions

- Accounting conventions are interchangeable used with accounting principles developed out of common practices. Hence the three words- concepts/ principles and conventions can be used interchangeably.
- This unit completely deals with the types of the Accounting principles/conventions/concepts-
  - Business entity concept ; Money measurement concept; Periodicity concept; Accrual concept; Matching concept; Going concern concept; Cost concept; Realisation concept; Dual aspect concept; Conservatism; Consistency; Materiality
- In total you will be able to understand these concepts very easily with examples, and in the exam they will test you with 2 mark questions on these concepts.
- **Business entity concept-** The business is a separate legal entity and is not related with the owner meaning the concept is that there shall be a distinction in the transactions which are related to the business and that of the owner. Personal transactions of the owner shall be treated as DRAWINGS and deducted from the capital.

Unit 2-Accounting concepts, principles and conventions

- **Money measurement concept**- Money is always the measurement scale for medium of exchange. Where those items which are measurable in terms of money are only being brought into the accounts. Other items however material they are cannot find a place in the accounts from the very definition of the accounts. If there is more than one currency- then using the conversion rates- all the money is converted into home currency value.
- **Periodicity concept-** The basic accounting states that a company shall be based on going concern concept, but the fact is that we cannot wait till such time when we can prepare the financial statements. Hence, for the accounting purpose the going concern is split into fewer periods- generally into period of 12 months (1 year) – finite time frame.
- **Accrual concept-** This is also called as mercantile system of recording the transactions where in all the transactions irrespective of paid or received in cash are recorded for the current accounting period- For ex- Outstanding / accrued.

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- **Matching concept-** The logic here is that every expense should have a revenue- technically meaning that all the items in the final accounts shall be matched. This is based on the periodicity and the accrual concept. All the revenue recognized for the period shall have matching expenses to arrive at the periodic profit.

- **Going concern concept-** This means that the business is opened today with the only intention to take it forward indefinitely. The financial statement should be prepared on the basis of this assumption. Where the concern is about to be closed down then the preparation of the financial statements will follow a different approach.

- **Cost concept-** Based on this concept the value of an asset will be always recorded at the historical cost or acquisition value. Generally there are various reasons such a inflationary trends, non availability of replacement which will affect this concept.

- **Realization concept-** This is based on the principle that showing at the cost might not give a correct picture instead if the realization value is considered it might be a prudent value. But only after the realization, the value is recorded. If there is any loss anticipated- it is given effect of

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- **Dual aspect concept-** This is the fundamental concept which tells that- there is a debit and credit for each transaction- debit and credit shall tally after each transaction. Every transaction shall affect two accounts each with debit and credit respectively.
- **Conservatism-** This states that losses shall be provided for and the incomes/gains to be recorded upon the actual realization. This is also concerned with the realization concept. Under this concept the profits are always understated since we do not recognize the gains until realization.
- **Consistency-** Where any accounting policy has been adopted by an organization- it shall be followed consistently year on year. We cannot follow different policies for different years, which leads to non-uniformity of financials over the years.
- **Materiality-** Based on the profitability or the financial position of any business, the transactions which are significant in total value shall be recorded and reported as per this concept. This is a subjective concept which is based on the knowledge, understanding and principles of accountant of an entity.

Unit 2-Accounting concepts, principles and conventions

- **Fundamental accounting assumptions-** Going concern, Consistency and Accrual
- **Qualitative characteristics of financials statements-**
  - **Understandability**- FS should be understandable, where ever complex items- they need to be mentioned in form of notes to accounts.
  - Relevance- FS has to provide information which is relevant for present decision making and forecasting various other items for future
  - Reliability- FS should provide reasonable and reliable information. They shall not have any material omissions or material misstatements.
  - Comparability- FS shall be comparable among the different periods and also with different enterprises.
  - Other characteristics are- Complete, prudent, substance over form, Materiality, neutrality, faithful representation, full and adequate disclosure.
  - Hence the financial statements at large are being prepared in accordance with the various accounting concepts/principles and conventions.

THANK YOU