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Accounting – Principles, Concept and Conventions

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Abstract: This paper depicts about the accounting principles ,concepts and conventions. Accounting provides financial information about a business organization.

Definition and introduction:

The worldview of accounting and accountants may certainly involve some unhelpful characters poring over formidable figures stacked up in indecipherable columns.

Accounting not only records financial transactions and conveys the financial position of a business enterprise; it also analyses and reports the information in documents called "financial statements."

The American Institute of Certified Public Accountants defines accounting as:

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

Recording every financial transaction is important to a business organisation and its creditors and investors. Accounting uses a formalised and regulated system that follows standardised principles and procedures.

Accounting may be defined as the process of recording, classifying, summarizing and interpreting the financial transactions and communicating the results there of to the persons interested in such information.

The job of accounting is done by professionals who have educational degrees acquired after years of study. While a small business may have an accountant or a bookkeeper to record money transactions, a large corporation has an accounts department, which supplies information to:

- Managers who guide the company.
- Investors who want to know how the business is doing.
- Analysts and brokerage firms dealing with the company's stock.
- The government, which decides how much tax should be collected from the company.

Accounting Principles

Obviously, if each business organisation conveys its information in its own way, we will have a babel of unusable financial data.

Personal systems of accounting may have worked in the days when most companies were owned by sole proprietors or partners, but they do not anymore, in this era of joint stock companies.

These companies have thousands of stakeholders who have invested millions, and they need a uniform, standardised system of accounting by which companies can be compared on the basis of their performance and value.

Therefore, accounting principles based on certain concepts, convention, and tradition have been evolved by accounting authorities and regulators and are followed internationally.

These principles, which serve as the rules for accounting for financial transactions and preparing financial statements, are known as the "*Generally Accepted Accounting Principles*," or GAAP.

GAAP (Generally Accepted Accounting Principles): It is a Technical concept that describes the basic rules, concepts, conventions and procedures that represent accepted accounting practices at a particular time.

The application of the principles by accountants ensures that financial statements are both informative and reliable.

It ensures that common practices and conventions are followed, and that the common rules and procedures are complied with. This observance of accounting principles has helped developed a widely understood grammar and vocabulary for recording financial statements.

However, it should be said that just as there may be variations in the usage of a language by two people living in two continents, there may be minor differences in the application of accounting rules and procedures depending on the accountant.

For example, two accountants may choose two equally correct methods for recording a particular transaction based on their own professional judgement and knowledge.

Accounting principles are accepted as such if they are (1) objective; (2) usable in practical situations; (3) reliable; (4) feasible (they can be applied without incurring high costs); and (5) comprehensible to those with a basic knowledge of finance.

Accounting principles involve both accounting concepts and accounting conventions. Here are brief explanations.

Accounting Concepts :

1. **Business entity concept:** A business and its owner should be treated separately as far as their financial transactions are concerned.

2. **Money measurement concept:** Only business transactions that can be expressed in terms of money are recorded in accounting, though records of other types of transactions may be kept separately.

3. **Dual aspect concept:** For every credit, a corresponding debit is made. The recording of a transaction is complete only with this dual aspect.

4. **Going concern concept:** In accounting, a business is expected to continue for a fairly long time and carry out its commitments and obligations. This assumes that the business will not be forced to stop functioning and liquidate its assets at "fire-sale" prices.
5. **Cost concept:** The fixed assets of a business are recorded on the basis of their original cost in the first year of accounting. Subsequently, these assets are recorded minus depreciation. No rise or fall in market price is taken into account. The concept applies only to fixed assets.

6. **Accounting year concept:** Each business chooses a specific time period to complete a cycle of the accounting process—for example, monthly, quarterly, or annually—as per a fiscal or a calendar year.

7. **Matching concept:** This principle dictates that for every entry of revenue recorded in a given accounting period, an equal expense entry has to be recorded for correctly calculating profit or loss in a given period.

8. **Realisation concept:** According to this concept, profit is recognised only when it is earned. An advance or fee paid is not considered a profit until the goods or services have been delivered to the buyer.

Accounting Conventions

There are four main conventions in practice in accounting: conservatism; consistency; full disclosure; and materiality.

Conservatism is the convention by which, when two values of a transaction are available, the lower-value transaction is recorded. By this convention, profit should never be overestimated, and there should always be a provision for losses.

Consistency prescribes the use of the same accounting principles from one period of an accounting cycle to the next, so that the same standards are applied to calculate profit and loss.

Materiality means that all material facts should be recorded in accounting. Accountants should record important data and leave out insignificant information.

Full disclosure entails the revelation of all information, both favourable and detrimental to a business enterprise, and which are of material value to creditors and debtors.

Key Differences Between Accounting Concept and Convention :

The difference between accounting concept and convention are presented in the points given below:

1. Accounting concept is defined as the accounting assumptions which the accountant of a firm follows while recording business transactions and preparing final accounts. Conversely, accounting conventions imply procedures and principles that are generally accepted by the accounting bodies and adopted by the firm to guide at the time of preparing the financial statement.
2. Accounting concept is nothing but a theoretical notion that is applied while preparing financial statements. On the contrary, accounting conventions are the methods and procedure which are followed to give a true and fair view of the financial statement.
3. While accounting concept is set by the accounting bodies, accounting conventions emerge out of common accounting practices, which are accepted by general agreement.
4. The accounting concept is basically related to the recording of transactions and maintenance of accounts. As against, the accounting conventions focus on the preparation and presentation of financial statements.
5. There is no possibility of biases or personal judgement in the adoption of accounting concept, whereas the possibility of biases is high in case of accounting conventions.

Conclusion:

To sum up, the accounting concept and conventions outline those points on which the financial accounting is based. Accounting concept does not rely on accounting convention, however, accounting conventions are prepared in the light of accounting concept**.**