

Introduction to Accounting Principles

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1. What is Accounting?

- **Definition:** Accounting is the systematic process of recording, summarizing, analyzing, and reporting financial transactions of a business.
- **Purpose:** To provide useful financial information to stakeholders for decision-making.

2. Importance of Accounting Principles

- Ensure consistency and reliability in financial reporting.
- Facilitate comparability of financial statements across periods and organizations.
- Help maintain transparency and accountability.
- Provide a framework for preparing financial statements.

3. Generally Accepted Accounting Principles (GAAP)

- A set of rules and standards that guide the accounting process.
- Used primarily in the United States.
- Ensures consistency, reliability, and comparability in financial reporting.

4. Key Accounting Principles

a. Economic Entity Assumption

- Business is separate from its owners or other businesses.
- Financial records must be kept distinct for each entity.

b. Monetary Unit Assumption

- Only transactions measurable in monetary terms are recorded.
- Assumes the currency is stable over time and ignores inflation.

Introduction to Accounting Principles

c. Going Concern Principle

- Assumes the business will continue to operate indefinitely.
- Financial statements are prepared under the assumption the business won't liquidate soon.

d. Cost Principle

- Assets are recorded at their original purchase cost.
- Cost is used as the basis for accounting, not market value.

e. Matching Principle

- Expenses should be matched with the revenues they help to generate.
- Ensures income statements reflect true profitability for a period.

f. Revenue Recognition Principle

- Revenue is recognized when it is earned, regardless of when cash is received.
- Focus on when the service or product delivery occurs.

g. Full Disclosure Principle

- All relevant financial information must be disclosed in financial statements.
- Ensures transparency to users of financial statements.

h. Conservatism Principle

- When faced with uncertainty, choose the option that results in lower profits or asset valuation.
- Avoids overstatement of financial health.

5. Basic Accounting Assumptions

- **Time Period Assumption:** Financial reporting should be done periodically (monthly, quarterly, annually).
- **Accrual Basis:** Revenues and expenses are recorded when earned/incurred, not necessarily when cash changes hands.

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6. Summary

- Accounting principles provide a standardized framework for recording and reporting financial activities.
- Adherence to these principles ensures financial statements are accurate, consistent, and useful for stakeholders.
- Understanding these foundational concepts is essential for anyone involved in financial reporting or analysis.