LECTURE 6

ACCOUNTING CONCEPTS AND CONVENTIONS

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LEARNING OUTCOMES

Upon completion of the lecture, the students should be able to:

- Describe the assumptions which are made when recording accounting data.
- Explain the concept of objectivity and subjectivity in the accounting context.
- Explain the underlying concepts and conventions of accounting.

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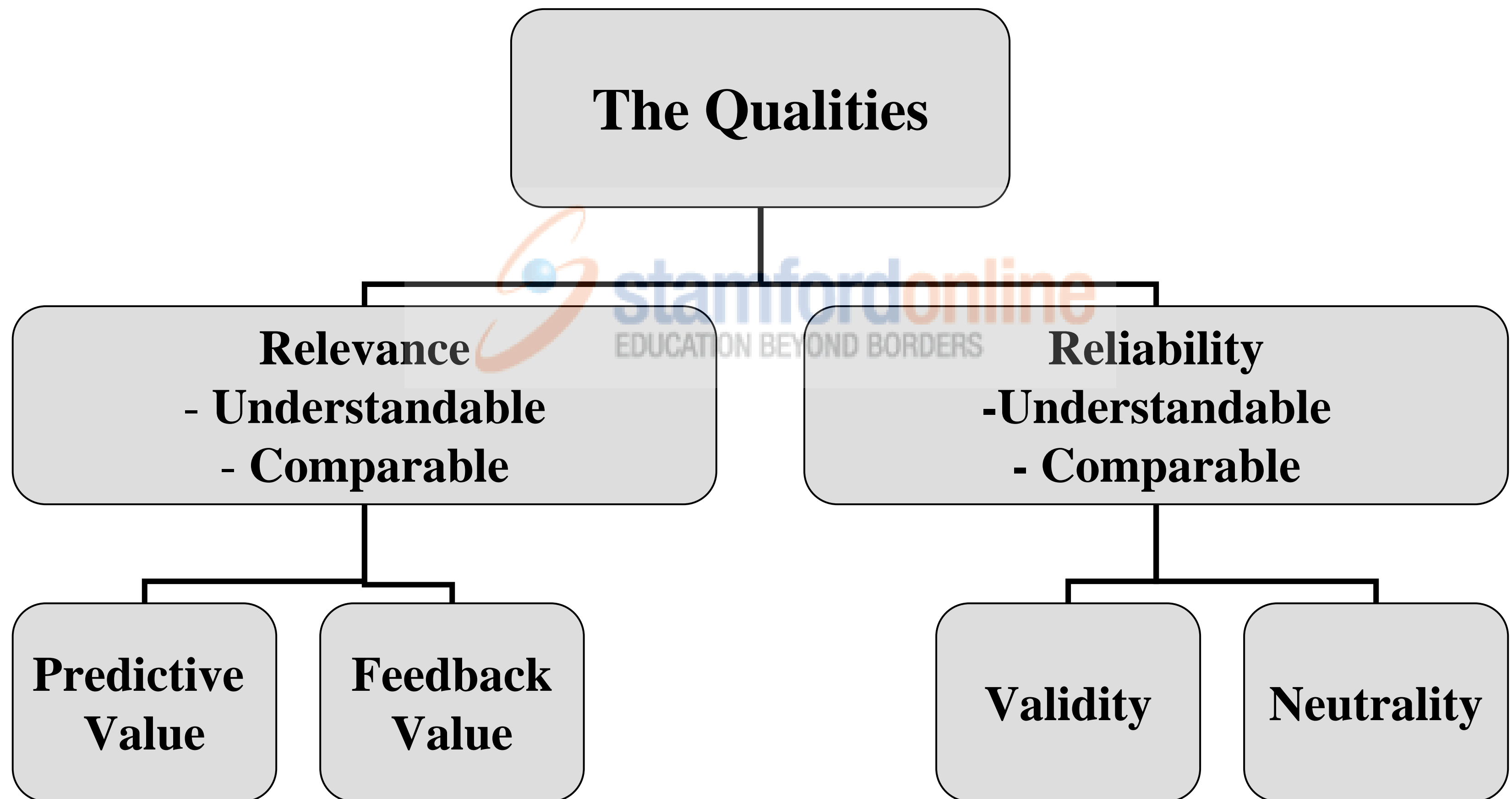
Qualities that Increase the Value of Information for Decision-making



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Underlying Concepts

- **Accounting Entity Concept**

  The transactions of each entity are accounted for separately from transactions of all other organisations and persons, including the owners of the business

- **Accounting Period Concept**

  Ensures that accounting information is reported at regular intervals [aids the comparison of business operations over time].

- **Stable-Monetary-Unit Concept**

  The accountant's basis for ignoring the effect of inflation and making no adjustments for the changing value of the ringgit or dollar.

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Accounting Principles

- **Relevance Principle**

  Provides that all relevant information should be included in the financial reports. Information is considered to be relevant if it assists readers in making decision.

- **Reliability [Objectivity] Principle**

  Requires that the accounting information can be dependable, that is verifiable by the people outside the business [independent experts].

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- **Comparability [Consistency] Principle**

  The information must be comparable from business to business and a single business's financial statements must be comparable from one period to the next.

- **Understandability Principle**

  The information should always be presented in a form which is as easily understandable as possible.

- **Going Concern Principle**

  Assume that the business will continue operating for the foreseeable future. This principle allows for the reporting of assets and liabilities as current and non-current.

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- **Cost Principle**

  States that assets and services are recorded at their purchase cost and that the accounting record continues to be based on cost rather than the current market value. The underlying basis for the cost principle is the reliability principle, where the actual cost of an asset or service is the objective evidence of its value.

- **Revenue Recognition Principle**

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  Provides guidance on the timing of the recording of the revenue and the amount of the revenue to be recoded. The general practice is that revenue should be recorded when it is earned. The three methods: point-of-sale method, point-of-production method, and point-of-collection method.

- **Matching Principle**

  This principle governs the recording and reporting of expenses. This principle goes hand-in-hand with the revenue recognition principle. The matching of the expenses incurred during the period against the revenues for the period reflects the profit for the period.

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- **Disclosure Principle**

  The business's financial statements should report enough information for the outsiders to make knowledgeable decisions about the business. The financial statements should report relevant, reliable, and comparable information about its economic affairs.