UNIT – 1

Introduction:

"Profit to a business is like food to human body." That is, the main object of any business is to earn profit. To earn profit, a businessman enters into a number of business transactions. As profit is earned from business transactions, if a businessman wants to find out how much profit he has earned from his business during a given period, he must be able to remember all the transactions of his business for that period. But it is not possible for any businessman to remember all the transactions of his business for a period, however good his memory may be. This has made him to keep a record of his business tractions in books of account. So, originally, accounting was introduced, as an aid to human memory, to have a permanent and systematic record of business transactions that would help a businessman to know easily and readily his business transactions, and the profit and the financial positions of his business.

Meaning:

Accounting is the process identifying, measuring, recording, classifying and summarising business transactions, analysing and interpreting the results thereof, and communicating the results of the interpretations to the end-users for decision-making.

Definitions:

The American Institute of Certified Public Accountants has defined accounting as "the art of recording, classifying and summarising, in a significant manner and in terms of money, transactions and events which are, in part at least, of financial character ad interpreting the results thereof:".

According to the American Accounting Association, "Accounting is the process of identifying, measuring and communicating economic information to permit informed judgements and decisions by users of the information:.

Objectives:

The main objectives of accounting are:

1. To maintain proper records of business transactions
2. To ascertain the profit or loss of the business
3. To know the sources of revenue and the items of expenses
4. To ascertain the financial position of the business
5. To ascertain the amounts due to the business, and the amounts due from the business
6. To ensure effective control over the performance of the business
7. To prevent errors and frauds
8. To satisfy legal requirements
9. To make financial information available to various groups of persons

Functions of Accounting:

1. Recording business transactions: The main and primary function of accounting is to keep systematic record of business transactions.

2. Indicating earning capacity and financial position: Preparation of final accounts which include trading, profit and loss account and balance sheet is also a function of accounting.

It is on this basis that the earning capacity and financial position of the unit concerned can be ascertained.

3. Satisfying Government Agencies: One of the functions of accounting is to satisfy various Government agencies. In Income-tax, tax is charged on net profit and net loss is allowed to be carried forward for writing it off out of the income of future years, hence it is through accounting, that reliable information regarding profit or loss may be obtained and this may provide satisfaction to the taxation authorities.

4. Complying legal requirements: In case of registered companies, auditing is not possible without accounting; hence accounting has to be made of such a standard as to comply with the legal requirements.

5. Assisting the Management: Accounting provides valuable information to the management in performing various management functions viz., planning, organising, controlling, co-ordinating, decision-making etc. Decision-making of management is mainly based on the results disclosed by accounting.

6. Protecting the assets: When the accounts are properly maintained, assets will be used only in the interest of the enterprise. Without receipt of adequate amount, the assets will not be disposed of. All this is possible through proper accounting.

7. Depiction of true financial position: Another function of accounting is to depict true financial position of the business as a whole.

Advantages of Accounting

Following are the advantages of accounting

1. **Advantages to Businessman**:
    - It helps in acquiring financial information about the business
    - It helps in buying and selling process of business
    - Comparison of the accounts of various years assists in getting various beneficial information
    - Properly maintained accounts act as a good proof in a court of law
    - It helps in acquiring loan
    - It helps determining the amount of goodwill

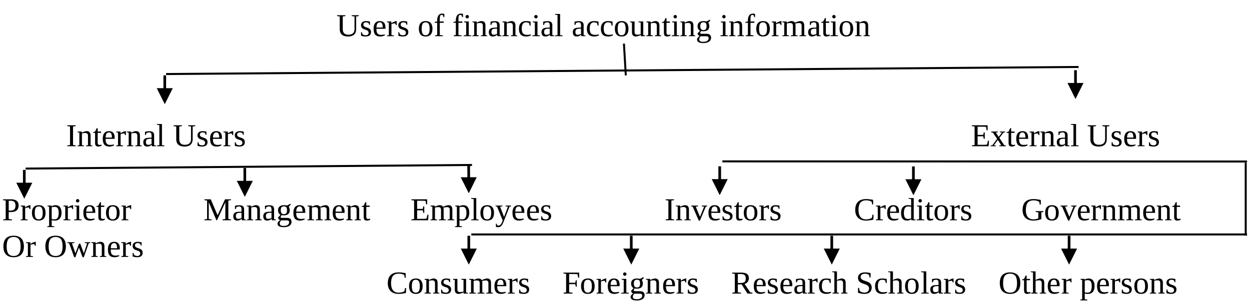
2. **Advantages to the employees**: Accounting record helps the employees in all matters related to their wages, salaries, bonus, etc.
3. **Advantages to the persons concerned**: All the persons, who are directly or indirectly concerned with the business, are benefitted by it, as it removes doubts about the amounts to be received or paid.
4. **Advantages to Government** :
    - Financial assistance is provided by the government on the basis of accounting record
    - Country's industrial progress can be judged on its basis
    - It helps in making assessment of total income for the purpose of determining taxes
    - It helps in providing licenses
5. **Advantages to Management**: Management always remain keen in knowing the result of its efforts which is indicated by accounting record. It is on this basis that they frame new policies, alter existing methods and formulate new schemes and control business activities

6. **Advantages to Investors**: If the investors wants to purchase the shares of the company of eager to made investment by other means in the business unit, they becomes eager to know the past and present financial position, earning capacity, liquidity position of the unit concerned. They also makes an interpretation about the future growth of the unit and all this he does on the basis of accounting record
7. **Advantages to competing concerns:** Competing concerns always remain keen to know the financial position of all those units whom they regard as their competitors. Accounting record helps the competitors to know the financial position of other business.
8. **Advantages to the new entrepreneurs:** Accounting records provides information about the earning capacity and financial position of the business unit to those entrepreneurs, who want to start business in a particular line. It helps them in deciding whether to start that type of business or not

Limitations of Accounting

1. The items expressed in monetary terms are recorded in the accounting where as the items which are nonmonetary nature is not recorded in accounting.
2. Sometimes accounting data are recorded on the basis of estimates and which could be inaccurate.
3. Accounting can be manipulated and biased.
4. Cost concept is adopted in accounting. Changing prices aren't considered. This is very strong limitation f accounting
5. Provision is made for prospective losses, but prospective profits are not taken into account. As a result, the exact state of affairs of the business is not revealed
6. In financial statements, only material items are disclosed in detail. Insignificant items are not disclosed.
7. Accounting methods or systems are static, and not flexible
8. Accounts are influenced by the personal judgements of the accountant. So, accounting records are subjective, and not objective.

Users of financial accounting information and their needs



Internal Users:

The owners and persons working in the organisation at managerial levels and employees are considered as internal users of accounting information

a) Proprietors /Owners : Accounting information helps the proprietor to know the earning capacity, financial position, future prospects of the enterprise

b) Management: Management is a group of people who are responsible for using the resources and managing the affairs of an entity to achieve the goals and objectives. Managers perform many managerial functions such as planning, controlling, directing, measuring, evaluating and taking corrective actions. Accounting information is of great relevance to the management for planning, controlling, co-ordination organising, budgeting, decision-making and for performing many activities. Thus, management can improve the efficiency, increase production and increase profitability by using accounting information in an appropriate manner.

c) Employees: Employees always feel that proprietor makes huge profit while their remunerations are limited, this doubt is removed by accounting information. On the basis of profit and loss account of the current year, they can know current year's profit and can compare it with the profit of the previous year. In case the profitability is higher, they can make a demand for bonus, increase in remuneration and retirement benefit schemes etc.

Employees are also eager to know about the continuance of the organisation in future for unlimited period because it will result in the continuance of their services, therefore, in the basis of balance sheet they can ascertain their job security and stability.

External Users:

The persons who are neither proprietor nor employees, but they have interest in business activities are called external users. They use accounting information for various purposes according to their requirements.

a) Creditors: Persons who supply goods on credit or provide long-term finance are termed as creditors. They need information to determine whether the concern will be able to pay their principal and interest as and when due.

b) Investors: It is only after knowing the profitability and sound financial position that potential investors take decision about making investment and present investors to continue investment in an enterprise. Accounting information is of great use to them in this connection specially in making judgement for their returns on investments.

c) Consumers: Consumers are interest in the prices of the gods and services rendered by an enterprise. This price decision is based on cost of production plus estimated margin of profit; hence consumers are interested in accounting information with which an idea of price structure can be made.

d) Government: Accounting information is used by the government for the following purposes:
   - Fixation of tax rates and introduction of new taxes
   - To assess whether the unit is going to become sick
   - To compute national income
   - To prepare national accounts
   - To know industrial growth of the country

e) Research Scholars: Accounting information helps research scholars who wants to make a study into the financial operation of a particular firm.

f) Foreigners: Now, the entire world has become one market due to rapid growth of means of transport and communications. Some foreign companies are eager to know the profitability and financial position of certain enterprises. On the basis of this information they may make an opinion about import, export and also about merger and business takeovers.

g) Other Persons: Many other persons are also interested in accounting information for instance:
    i. Entrepreneur: an entrepreneur is eager to know the profitability and financial position of those enterprises which are already in an industry. It is only after knowing their position he will make up his mind whether to start similar enterprise or not.
    ii. Taxation Authorities: Taxation authorities needs and accounting information for determining various tax liabilities, i.e., income tax, sales tax, etc.
    iii. Competitors: The persons, who want to compete with a particular enterprise, want to know its position on the basis of its accounting record.
    iv. Trade Associates: these associations compare the performance of their members' units and then, if need be, demand concessions or exemptions from the government in taxation and other spheres
    v. Stock Exchanges: They require accounting information in connection with listing of securities and other spheres connected with various dealings in stock exchanges.

Accounting System:

Accounting system refers to the way in which business transactions are recorded in the books of accounts of a business.

Accounting systems can be classified into two systems. They are:

1. Single entry system of accounting
2. Double entry system of accounting

Single Entry System:

It is s system of accounting under which a complete record of each and every transaction is not kept.

Under, this system, for some transactions, both the aspects are recorded, for a few transactions, none of the aspects is recorded, and for most of the transactions, only one aspect is recorded.

Advantages of Single –Entry System:

The main advantages of single-entry system are:

1. It is a simple method of recording business transactions, because an elaborate accounting procedure is not involved in this system.
2. The maintenance of accounting records under this system does not call for adequate skill and knowledge of principles of accounting on the part of account keepers.
3. It is less costly when compared to the double entry system, because fewer books are maintained under this system
4. Ascertainment of profit or loss under this system is much easier

Disadvantages of Single – Entry System:

1. This system is an incomplete system of book-keeping, because the two aspects of each and every transaction are not recorded in the books of account under this system
2. Counter check of entries is not possible
3. It is not possible to prepare a trial balance and verify the arithmetical accuracy of the books of account

4. This system does not provide any useful information about the sources or causes of profits or losses.

Double - Entry System:

The system of making two or double entries of equal value in two different accounts in opposite sides in the books of each of the contracting parties is known as the double –entry system of accounting.

Advantages Double - Entry System:

1. It provides a complete or full record of all the business transactions
2. It is possible to prepare a trial balance and check the arithmetical accuracy of books of accounts
3. It is possible to prepare a profit and loss account and find out the true net profit or net loss for a particular year
4. The information about assets, liabilities and capital are available under this system, it is possible to prepare a balance sheet and ascertain the true financial position of the business on any particular date.
5. When the books of accounts are maintained on the double-entry system, it becomes easy for a business concern to satisfy the income-tax and sales tax authorities about the accuracy of the business transactions

Disadvantages Double - Entry System:

1. It is a complicated and difficult system
2. This system involves the maintenance of a number of account books. So, it is costly
3. This system requires strict adherence to the principles or rules of accountancy
4. This system also does not disclose all the errors committed in the books of account

Classification of Accounts

Every business concern deals with other persons, firms or companies. Secondly, a business concern has certain properties or assets, such as goods, cash etc. in which or with which the business is carried on. Thirdly, it may incur certain expenses, such as salaries, rent, etc., and may earn some incomes, such as commission interest, etc.

From the above, it is clear that every business concern has three classes of transactions, i.e., transactions relating to persons, transactions relating to assets and transactions relating to expenses and incomes. So, a concern must maintain accounts for all these three classes of transactions.

The accounts maintained by a business concern for these transactions are as follows:

Classification of Accounts

Personal Accounts | Impersonal Accounts

Real, Asset or Property Account   Nominal or Fictitious Accounts

Personal accounts:

These are the accounts of persons with whom a concern carries on business. Personal accounts may be

a) Natural Personal Accounts: These are the accounts of human beings, such as Ram's Account, Sita's Account, Janakiram's Account, etc.
b) Artificial personal Accounts: These are the accounts of artificial or legal persons, i.e., accounts of partnership firms, companies, clubs, associations, banks, Government institutions, schools and colleges, etc., such as the Canara Trading Company's Account, The National trading company Ltd.'s Account.
c) Representative Personal Accounts: These are the accounts of accrued expenses, outstanding expenses, prepaid expenses, accrued incomes, outstanding incomes etc. These accounts are called representative personal accounts, as they represent certain persons behind them.

Real, Asset or Property Accounts:

These are the accounts of properties, assets or things owned by a concern with which the business s carried on. Real or asset accounts may be:

a) Accounts of tangible assets such as goods account, cash account, furniture account vehicles account, machinery account, buildings account, land account, etc.
b) Accounts of Intangible assets such as goodwill account, patent rights account, copyright account, etc.

Nominal or Fictitious Accounts:

These are the accounts of the expenses and losses which a concern incurs, and incomes and gains which a concern earns in the course of its business. These accounts are called nominal accounts, because they do not really exist. They exist only in names. Nominal accounts may be:

a) Revenue or income accounts i.e., accounts of revenues, income, gains or profits, such as commission earned, interest received, discount received etc.
b) Expenses accounts i.e., accounts of expenses or losses, such as salaries paid, rent paid, discount allowed, bad debts, etc.

Rules of Debit and Credit

Every business transaction has two aspects, i.e., receiving of some benefit called the receiving aspect, and the giving of some other benefit called the giving aspect.

The fundamental or general rule of the double entry system of accounting is that the account which receives the benefit of the transaction must be debited and the account which gives the benefit of the transaction must be credited. But, the general rule for debit and credit is adjusted in accordance with the types of accounts and three sets of rules are laid down for the three classes of accounts.

The general rules for debit and credit are as follows

Personal Accounts:

The account of the person who receives the benefit of the transaction from the business should be debited, and the account of the person who gives the benefit of the transaction to the business should be credited.

Real or Asset Accounts:

The account of an asset which comes into the business should be debited and the account of an asset which goes out of the business should be credited

Nominal or Fictitious Accounts:

The account of an expense or loss of the business should be debited and the account of an income or gain of the business should be credited

The above rules for debiting and crediting various accounts may be summarised as follows:

1. **Personal Accounts:**	Debit the receiver And Credit the giver
2. **Real or Asset Accounts:**	Debit what comes in and Credit what goes out
3. **Nominal or Fictitious Accounts:**	Debit expenses and losses and Credit incomes and gains

Journal

Introduction:

The book of original entry under the conventional method or theoretical method of accounting is the journal.

Meaning:

The term journal is derived from the French work 'jour' which means a day. It is a book of original entry in which all transactions are first recorded chronologically from the source documents.

Objectives of Journal

The important objectives of journal are:

a. To record each day's transactions the same day.
b. To provide a chronological record of all business transactions.
c. To avoid the necessity of making entries in the ledger immediately after the occurrence of the business transactions.
d. To serve as a book of original or first entry.
e. To provide a complete record of each transaction in one place.
f. To help in the preparation of various accounts in the ledger.
g. To serve as a legal evidence or proof of business transactions by containing original entries of the transactions.

Advantages of Journal

The important advantages of journal are

1. It provides the chronological record of transactions.
2. It facilitates quick and easy reference to any transaction.
3. It gives the complete story of a transaction in any entry.
4. It reduces the possibilities of errors, as the amounts to be debited and credited are written side by side in the journal
5. By providing narration, journal helps one to understand the purpose and the nature of the entry

Limitations of Journal

The limitations of journal are:

1. If all the business transactions are recorded in the journal, the journal will become very bulky
2. The work of writing up of the journal is laborious and tedious
3. It will not provide final information on the various matters of business

Form of Journal

The journal is ruled as follows:

Date	Particulars	L.F	Dr. Rs.	Cr. Rs.

Ledger

Introduction

After all the transactions are journalised, the entries in the single journal are posted or transferred to the appropriate account in the ledger, periodically, i.e., weekly, fortnightly, monthly or quarterly, to know the exact position of each account on any particular date.

Meaning

It is a summary statement of all the transactions relating to a particular person, asset, expense or income which have taken place during a given period of time.

Objectives

1. To provide an analytical record of business transactions.
2. To provide a permanent record of all the transactions of the business
3. To help in the preparation of all the transactions of the business
4. To help in the preparation of the trial balance
5. To help in the preparation of final accounts

Advantages

1. A ledger is a permanent record of all the transactions of all the transactions of a business
2. It provides complete information about all accounts in one book.
3. It is a summarised and classified record of transactions of the same nature. As such, a ledger, which contains all the ledger accounts, is helpful in knowing the cumulative effect of all the transactions relating to each person, thing or service, i.e., final position or balance of each account on any particular date.
4. It is helpful in preparing the trial balance.
5. It facilitates the preparation of final accounts.
6. It helps to ascertain the assets and liabilities of the business and their values

Form of Journal

A Ledger account is ruled as follows:

Dr. **Cr.**

Date	Particulars	J.F	Amount Rs.	Date	Particulars	J.F	Amount Rs.

Trial Balance

Introduction:

The main objective of accounting is to ascertain the profit or loss and the financial position of the business. The profit or loss and financial position of the business can be ascertained by preparing the final account. The final accounts have to be prepared on the basis of various accounts in the ledger. The ledger accounts are spread over many pages of the ledger or over different ledgers. So, it is very difficulty to the accountants to ascertain the balances of various ledger accounts. To overcome this difficulty, a list of the balances of various ledger accounts, called the trial balance, is prepared by the accountant as on the closing date of the accounting year.

Meaning:

Trial balance is a list of debit and credit totals, or a list of debit and credit balances, of all the ledger accounts prepared on any particular date to verify whether the entries in the books of account are arithmetically correct.

Definition:

Acc. to J.R. Batliboi, "Trial balance is a statement, prepared with the debit and credit balances of ledger accounts to test the arithmetical accuracy of the books".

Acc. to R.N. Carter, "A trial balance is a schedule or list of balances, both debit and credit, extracted from the accounts in the ledger and including cash and bank balances from the cash book".

Acc. to Spicer and Pegler, "A trial balance is a list of all the balances standing in the ledger accounts and cash book of a concern at any given date".

Objectives of Trial Balance:

1. To bring the balances of all the accounts in the ledger in one place so that the balance of any particular account can be found easily
2. To check the accuracy of the books of account
3. To help in locating errors
4. To help in the preparation of final accounts
5. To help in the making of adjustments while preparing final accounts

Advantages:
1. It facilitates easy and quick preparation of final accounts
2. It ensures that the final accounts reveal the true results
3. The balances of ledger accounts found in the trial balance serve as rough guide as to the state of affairs of the concern
4. It serves as an aid to management
5. The agreement of the trial balance is prima facie evidence of the proper application of the principle of double-entry system

Limitations:
1. It can be prepared only in those concerns where double-entry system of accounting is adopted
2. Tallied trial balance is not a conclusive proof of the accuracy of the books of account, because certain types of errors remain even when the trial balance tallies.
3. It is not a part of books of books of accounts

ACCOUNTING PRINCIPLES

INTRODUCTION:

A science is an organized body of knowledge, consisting of general principles having universal application. As accounting is a science, it has some general principles having wide application.

DEFINITION AND MEANING:

In the words of A. W. Johnson, “Accounting principles are the assumptions and rules of accounting, the methods and procedures of accounting and the application of these rules, methods and procedures to the actual practice of accounting”.

Accounting principles are generally decided rules, derived from the basic accounting concepts, which are followed by accountants universally in writing up the accounts and also in preparing the financial statements of business concerns. In short, accounting principles are rules of action or conduct which are adopted by accountants universally, while recording accounting transactions and preparing financial statements.

Classification of Accounting Principles or Kinds of Accounting Principles:

Accounting principles have been classified as:

- ACCOUNTING CONCEPTS
- ACCOUNTING CONVENTIONS

ACCOUNTING CONCEPTS

The term concept means idea or thought. So, accounting concepts are the fundamental ideas or basic assumption s underlying the theory and practice of accounting. In other words, accounting concepts are the broad working rules of accounting activity.

Benefits of accounting concepts:

a. Accounting concepts guide the identification of transactions to be accounted for(i.e., to be recorded).
b. They make accounting convey the same meaning to the end – users of accounting information as far as practicable.
c. They also help in bringing about uniformity in the practice of accounting.

Important accounting concepts

There are a number of accounting concepts. The important accounting concepts are:

1. Money measurement concept
2. Separate entity concept
3. Going-concern concept
4. Cost concept
5. Dual aspect concept
6. Accounting period concept
7. Objective evidence concept

8. Realization concept
9. Accrual concept
10. Matching concept
11. Legal aspect concept

1. **Money measurement concept or common denominator concept**:

   The money measurement concept implies that, in accounting, a record is made only of those transactions or events which can be measured and expressed in the terms of money. Non – monetary events like the good quality of the products produced by the concern, the team-work is found in concern, etc. are not recorded, though they are also material events, as they cannot be measured and expressed in terms of money.

2. **Separate entity concept, business entity concept, economic entity concept or accounting entity concept:**

   Business entity concept means that, in accounting, every business undertaking, whether it is a joint stock company or a partnership firm or a sole trading concern, is regarded as a distinct unit or entity apart from the owners who own it, and so, the business and the proprietors who own the business are regarded as two separate entities capable of entering into transactions with each other.

   This concept also means that, as the business and the proprietors of the business are two separate entities, the transactions of the business are distinguished from those of the proprietors, and in the books of the business, only the transactions of the business, and not the private transactions of the proprietors, are recorded.

3. **Going- concern concept or concept of continuity**:

   The going concern concept means that, in accounting, an enterprise is regarded as a going concern. There is neither the intention nor the necessity to wind up the concern in the foreseeable future. It may be noted that this concept does not mean permanent continuance of a business. All that it means is that a business enterprise will continue to operate for a fairly long period of time.

4. **Cost concept or historical cost concept**:

   The cost concept means that an asset acquired by a concern is recorded in the books of accounts at cost. The market price of the asset is ignored, and it is its cost price that forms the basis for all subsequent accounting for that asset

   .

5. **Dual aspect concept or accounting equation concept**:

   Every business transaction always results in receiving of some benefit of some value and giving of some other benefits of equal value. For instance, when a business purchases goods for cash, it receives goods of some value and gives cash of equal value. Similarly, when it sells goods for cash, it receives cash of some value and gives goods of equal value. Thus, every business transactions involve dual or double aspects of equal value.

So, in accounting, a recorded is made of the dual or two aspects of each transaction, and this called dual-aspect concept

6. **Accounting period concept or periodicity of accounts**:

   The accounting period concept means that, for measuring the financial results of a business periodically, the business or working life of an undertaking is split into convenient short periods of time called accounting periods, and profit or loss and financial position of the business are ascertained at the end of each accounting period by preparing financial statements.

7. **Objective evidence concept**:

   This concept means that all accounting entries should be evidenced and supported by source documents or business documents, such as invoices, vouchers, etc. This concept also means that the evidences must be completely objective and must be subject to verification by auditors.

8. **Revenue realization concept or revenue recognition concept:**

   The revenue realization concept means that revenue is earned from the sale of goods or from provision of services to customers, and revenue is to be recognized or considered to be realized only when goods or services are transferred to a customer and the customer becomes legally liable to pay for them. So, when an order is received from a customer, it does not mean that revenue is realized or earned.

9. **Accrual concept**:

   The accrual concept means that when a transaction has been entered into, its consequences will certainly follow. So, all transactions must be brought into record, whether they are settled in cash or not. It suggests that an accountant must treat as revenues all those items for which there are the legal right to receive, although cash might not have been received for them.

10. **Matching concept or periodical matching concept**:

    Profit is the result of two factors or items viz., revenues and expenses. So, for the measurement or determination of the profit or loss, these two factors are matched, and the resultant balance is taken as the net profit or the net loss. If the revenues exceed the expenses, the resultant balance is taken as the net profit. On the other hand, if the expenses exceed the revenues, the resultant balance is taken as the net loss. thus, the net profit or net loss of a business is determined by matching the expenses with the revenues.

ACCOUNTING CONVENTIONS

Accounting conventions are the customs or practices which have been in force for a long period and which guide the accountants, while preparing financial statements. In other words, they are the customs, usages or practices followed by accountants as a guide in the preparation of financial statements.

The important accounting conventions are:

1. Convention of materiality
2. Convention of conservatism
3. Convention of consistency
4. Convention of full disclosure

1. Convention of Materiality:

The convention of materiality means that, in accounting, a detailed record is made only of those business transactions which are material to the users of accounting information. No detailed record need be made of transactions which are trivial, as the work of recording the minute details of such transactions is not justified by the usefulness of the result.

2. **Convention of conservatism**:

The convention of conservatism means the convention of caution, prudence or the policy of playing safe. In other words, it means that, in the accounting records and the financial statements of a business, all the prospective losses, risks and uncertainties should be taken note of and provided for, but prospective profits should be ignored. In short, "provide for all possible losses, but anticipate no profits" is the implication of this principle.

3. **Convention of consistency**:

The convention of consistency signifies that the accounting practices and methods should remain consistent from one accounting year to another. For instance, when once a particular method of depreciation is adopted for a particular fixed asset, the same methods should be followed for that asset year after year. Similarly, when once stock-in-trade is valued at cost price or market price, whichever is lower, the same practice should be continued for all the years.

4. **Convention of full disclosure**:

The convention of full disclosure means that the material facts must be disclosed in the financial statements with sufficient details. the idea behind this convention is that the financial statements are essentially meant for external users. It is on the basis of the information conveyed by the financial statements that the external users make decisions. As such, the financial statements should disclose all the materials facts with as much details as possible. Exclusion of material facts makes the financial statements incomplete and unreliable.

IFRS:

The International Financial Reporting Standards (**IFRS**) are accounting standards that are issued by the International Accounting Standards Board (IASB) with the objective of providing a common accounting language to increase transparency in the presentation of financial information.

The following are the objectives of IFRS:

- To establish a universal language for the companies to prepare the accounting statements.
- To establish accounting rules to make it easier for the stakeholders to interpret the financial statements, irrespective of the business location.
- Make the accounting statements credible and transparent.
- To assist companies appropriately categorize and report financial data.
- It makes international comparisons and analysis an easy task.

Advantages of IFRS

1. Focus on investors

a)The first factor is that IFRS promise more accurate, timely and comprehensive financial statement information that is relevant to the national standards. And the information provided by financial statements prepared under IFRS tends to be more understandable for investors as they can understand the financial statement without the necessity of other sources which makes investors more informed

b)Due to harmonization and standardization of reporting standards under IFRS, the investors do not need to pay for processing and adjusting the financial statements to be able to understand them, thus eliminating the fees of analysts. Therefore, IFRS reduces the cost for investors.

2. Loss recognition timeliness

Recognising the loss immediately is one of the key features of IFRS as it is not only the benefit for the investors, but also for the lender and other stakeholders within the company.

The increased transparency and loss recognition of IFRS, usually increases the efficiency of contracting between companies and their management, which also enhances the corporate governance.

3. Comparability

The convergence to IFRS has improved the comparability of financial statements in the EU. This has been achieved through having the same reporting standard under a single market, the EU.

As all companies, preparing their consolidated financial statements, have been reporting under one reporting standard have improved the comparability not only for investors, but also all stakeholders who use the financial statements.

4 Standardization of accounting and financial reporting

The most mentioned factor about the advantages of IFRS has been the standardization of financial reporting which eventually improves the comparability of financial statements in major financial markets. This also removes the trade barrier, as this was one of the key factors as why the EU has been trying to adopt single reporting standards.

5 Improved consistency and transparency of financial reporting

This factor can also be mentioned as one of the crucial advantages of converting to IFRS as it makes the EU member countries to be consistent not only on macroeconomic aspects, but also on financial reporting which improves relationship between investors and companies among member countries.

6 Better access to foreign capital markets and investments

As thousands of companies in Europe and other joining countries across the world has already created a huge base for IFRS adoption, it also improves the companies to access to financial markets by having the financial statements prepared under one reporting standards.

One of the main reasons for converting from previously used GAAP to new IFRS was for improving comparability in international financial markets, thus increasing the focus on investors.

The Disadvantages of Adopting IFRS

- It would increase the cost of implementation for small businesses. ...
- It would lead to concerns with standards manipulation. ...
- It would require global consistency in auditing and enforcement. ...
- It would increase the amount of work placed on accountants.