

Accounting

Accounting is the **recording of financial transactions** along with storing, sorting, retrieving, summarizing, and presenting the results in various reports and analyses. Accounting is also a field of study and profession dedicated to carrying out those tasks.

Accounting or accountancy is the measurement, processing, and communication of financial and non financial information about economic entities such as businesses and corporations

Book keeping

- Bookkeeping is the recording of financial transactions, and is part of the process of accounting in business and other organizations. It involves preparing source documents for all transactions, operations, and other events of a business.
- The primary purpose of bookkeeping is to record the *financial effects* of transactions. An important difference between a manual and an electronic accounting system is the former's latency between the recording of a financial transaction and its posting in the relevant account. This delay, which is absent in electronic accounting systems due to nearly instantaneous posting to relevant accounts, is characteristic of manual systems, and gave rise to the primary books of accounts—cash book, purchase book, sales book, etc

Difference between Accounting and book keeping

Bookkeeping	Accounting
Bookkeeping is a foundation/base of accounting.	Accounting uses the information provided by bookkeeping to prepare financial reports and statements.
Bookkeeping is one segment of the whole accounting system.	Accounting starts where the bookkeeping ends and has a broader scope than bookkeeping.
The result of the bookkeeping process is providing input for accounting.	The result of accounting is preparing financial statements for making informed decisions and judgments.
The purpose of bookkeeping is to maintain a systematic record of financial activities and transactions chronologically.	The purpose of accounting is to report the financial strength and obtain the results of the operating activity of a business.

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The objective of bookkeeping is to summarise the effect of all financial transactions of a business for a given period.

The objective of accounting is to interpret and analyse financial information for informed decisions.

The person responsible for bookkeeping is called a bookkeeper.

The person responsible for accounting is called an accountant.

Bookkeeping is clerical in nature. The bookkeepers do not require any special knowledge or skill.

Accounting requires the skills of an accountant and knowledge of various accounting practices and policies.

Advantages and Disadvantages of Accounting

Advantages

- Maintenance of business records
- Preparation of financial statements
- Comparison of results
- Decision making
- Evidence in legal matters
- Provides information to related parties
- Helps in taxation matters
- Valuation of business
- Replacement of memory

Disadvantages

- Expresses Accounting information in terms of money
- Accounting information is based on estimates
- Accounting information may be biased
- Recording of Fixed assets at the original cost
- Manipulation of Accounts
- Money as a measurement unit changes in value

Various Users of accounting information

Internal users of Accounting information

Internal users are that individual who runs, manages and operates the daily activities of the inside area of an organization.

- Owners and Stockholders.
- Directors,
- Managers,
- Officers.
- Internal Departments.
- Employees
- Internal Auditor.

External users of Accounting information

- External users are those individuals who take interest in the account information of an organization but they are not part of the organization's administrative process.
- Examples of external users of accounting information are;
- Creditors.
- Investors.
- Government.
- Trading partners.
- Regulatory agencies.
- International standardization agencies.

Types of accounting principles

Accounting principle can be classified in the following manner

- **Basic accounting assumptions or concepts**
- **Basic accounting principles**

Basic Accounting assumptions or concepts

- **Going concern Assumptions or concept**
- **Consistency accounting of concept**
- **Accrual Assumption or Concept**

Basic accounting principles

- Business entity principle
- Money measurement
- Accounting period principle
- Principle of Dual aspect
- Principle of historical cost
- Principle of Matching
- Principle of Full disclosure
- Principle of Materiality
- Principle of Prudence and Conservatism

Limitations of Accounting

- *Measurability*
- One of the biggest limitations of accounting is that it cannot measure things/events that do not have a monetary value. If a certain factor, no matter how important, cannot be expressed in money it finds no place in accounting. Some very important qualities like management, loyalty, reputation, etc find no place on the balance sheet or the income statement.
- *No Future Assesment*
- The financial statements show the financial position of the firm on the date of preparation. The users of the statement are more interested in the future of the company in the short term and long term. However, accounting does not make any such estimates.
- And due to the dynamic nature of the business environment, a lot can change between such dates. Auditors sometimes do disclose the important events occurring after the balance sheet date to rectify these limitations of accounting.
- *Historical Costs*
- Accounting often uses historical costs to measure the values. This fails to take into consideration factors such as inflation, price changes, etc. This skews the relevance of such accounting records and information. This is one of the major limitations of accounting.
- *Accounting Policies*

- There is no global standard in accounting policies. In India, we follow the Accounting Standards. Americans follow the GAAP and then there are the international standards, namely the IFRS. And if a global company operates in more than one country, there may be confusion.
- Not all accounting policies follow the same line of thinking, and conflicts may arise due to this. It has long been said that the whole world must agree on uniform accounting policies but this has not happened yet.

- *Estimates*

- Sometimes in accounting estimation may be required as it is not possible to establish exact amounts. But these estimates will depend on the personal judgment of the accountant. And estimates are extremely subjective in nature. They are basically a person's guess of future events. In accounting, there are many cases where such estimates need to be made like provision of doubtful debt, methods of depreciation, etc.

- *Verifiability*

- An audit of the financial statements does not guarantee the correctness of such statements. The auditor can only assure that the statements are free from error to the best of his judgment.

- *Errors and Frauds*

- Accounting is done by humans, so there will always be the scope of human errors. There is also the fear of possible manipulation of accounts to cover up a fraud. Since fraud is deliberate, it is that much harder to spot. This is one of the most dreaded limitations of accounting.

FUNCTIONS OF ACCOUNTING

Historical or Stewardship Functions

- Communicating Financial Information
- Analyzing Financial Data
- Exhibiting Financial Affairs
- Finding Net Results
- Summarizing
- Classifying
- Recording of Financial Transactions

Managerial Functions

- Control of Financial Policy And Formation of Planning
- Preparation of Budget
- Cost Control
- Evaluation of Employees' Performance
- Prevention of Errors And Frauds

Source

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Book – book keeping and basic accounting by Dr SM Shukla