GAAP RULES

ACCOUNTING

The process of recording of business transactions is called accounting.

GAAP (Generally accepted accounting principles)

The rules that govern accounting are called generally accepted accounting principles (GAAP).

- The common set of accounting principles, standards and procedures.
- Combination of authoritative standards (set by policy board) and simply, the commonly accepted ways.

EXPLANATION

- ✓ Provides a fair financial image of the company.
- ✓ Provide with different information
    - Revenue reorganization
    - Balance sheet item classification
    - Outstanding share measurement.

3 MAIN CATEGIRIES OF GAAP

- **ASSETS:** An asset is an item of value owned by a business.
- **Liabilities:** Accounting liabilities are obligations of company, to transfer something of value to another party.
- **EQUITY:** Equity is the owner's value in and asses or group of assets.

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GAAP PRINCIPLES

The GAAP principles are divided into two categories.

1. **ACCOUNTING CONCEPT:**
   Accounting concept are basic assumption or conditions upon which science of accounting is based.
2. **ACCOUNTING CONVENTIONS:**
   Accounting conventions include those customs and traditions which are followed up by an accountant which preparing a financial statement.

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ACCOUNTING CONCEPT

1. ACCOUNTING CONCEPT

ACCOUNTING CINCEPT INCLUDE:

I. **SEPRATE ENTITIY CONCEPT:**
- ✓ It is helpful in keeping the business affairs strictly free from the effect of the affairs of the proprietor(s).
- ✓ Amount invested by the proprietor is shown as "liability".
- ✓ Amount paid for the personal expense of the proprietor are shown as drawing from the capital of the proprietor.

II. **MONEY MEASUREMENT CONCEPT:**
- ✓ Only the transactions which can be recorded in term of money are recorded.
- ✓ This is being used so as to provide a common yardstick (ie.money) for measurement.

III. **DUAL ASPECT CONCEPT:**
- ✓ Every business transactions have a dual affect i.e. it affect two accounts.
- ✓ This is based on accounting equations.

Assets = Liabilities

- ✓ Owner equity + outsider's equity = Assets
- ✓ This equations can be explained as "for every debt there is an equivalent credit"

IV. MATCHING CONCEPT:

It is the basis for recording expense incurred two steps

1. Identify all the expense incurred during the accounting period
2. Measure the expense and the match the expense against the revenues earned

Revenues – cost = net income or profit.

V. GOING CONCERN CONCEPT:

Business would continue to operate indefinitely in the future. Business will not cease doing business; neither will it sell its assets to pay off its liabilities.

VI. COST CONCEPT:

Assets and liabilities should be recorded at the historical cost i.e., cost as on acquisition.

VII. ACCOUNTING PERIOD CONCEPT:

Accounting period is the span of time, at the end of which financial statements are prepaid to throw light on the results of the operations at the relevant period and the financial position at the end of a relevant period.

VIII. REALIZATION CONEPT

The revenue principles govern two things:

1) When the record revenue.
2) Amount of revenue to record.

To be recognized, revenue must be:

EARNED: Goods are delivered or a service is performed.

REALIZED: Cash or claim to fast (credit) is received in exchange for goods and services rendered.

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2. ACCOUNTING CONVENTIONS

ACCOUNTING CONVENTIONS INCLUDE:

I. FULL DISCLOSER PRINCIPLES:

Financial statement should be honestly prepared and sufficiently, disclose information which is of material interest to proprietor, present and potential creditors and investors.

II. MATERIALITY:

Only material on significant details are to be recorded leaving the insignificant or prevent overburdening of accounts.

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