Accounting Standard 1

Cheat Sheet

OBJECTIVE

The objective of financial statements is to provide information about the financial position, performance and cash flows of an enterprise that is useful to a wide range of users, in making economic decisions.

The standard deals with what, where, which and how accounting policies should be disclosed. The accounting policies are set of principles, methods and procedures applied by management in preparation of financial statements.

Financial statements portray the effect of past events and transactions. Accounting policies and methods adopted by an enterprise, in turn, influence the effect of past events and transactions. Users must be able to compare the:

- financial statements of any one enterprise through time so that trends and movements in performance and position can be identified, and
- status of different enterprises for an evaluation of relative financial position and performance.

The Disclosure by an entity of it's accounting standards enables it's users to understand:
how the entity has been operating in the past
generalise that the trends will remain same in the future

Fundamental Accounting Assumptions

1. Going Concern

- Generally, an enterprise is assumed to be a going concern. This means the enterprise continues to operate for the foreseeable future.
- In other words, it is assumed that an enterprise neither intends nor is necessarily required to liquidate or cut down its scale of operations significantly.

2. Consistency

According to this assumption, the accounting policies followed by an enterprise to prepare its financial statements are consistent across different periods.

3. Accrual

As per this assumption, the revenues and costs are recognized as they are earned or incurred rather than when money is received or paid. Such accrued revenues or costs recorded in the financial statements concern to the periods to which they relate.

- *These concepts, which are fundamental to accounting, are the broad-based assumptions, underlying preparation of financial statements periodically. Financial statements are assumed to be prepared by adhering, among others, to these concepts.*
- *Unless any contrary position is unequivocally brought to notice, the user can validly presume that these principles have been followed. Consequently, if any one of these principles is not adhered to, such a fact ought to be disclosed.*

Areas in which Different Accounting Policies are Encountered

Following are the areas where different accounting policies may be adopted by different enterprises:

- Methods of depreciation, depletion & amortisation
- Treatment of expenditure during construction
- Conversion or translation of foreign currency items
- Valuation of inventories
- Treatment of goodwill
- Valuation of investment
- Treatment of retirement benefits
- Recognition of profit on long-term contracts
- Valuation of fixed assets
- Treatment of contingent liabilities
- However, the above list is not an exhaustive list.

Selecting an Accounting Principle

1. Prudence

- Profits are recognized as they are realized but loss if anticipated is provided for earlier.
- Eg., in determining the carrying amount of inventory, the profit margins are ignored and yet, the realisable value if less than cost is taken cognizance of.

2. Substance over Form

If information is to represent faithfully the transactions or events, it is essential that they are accounted for and presented in accordance with their substance and economic reality and not merely their legal form.

3. Materiality

The financial statements should disclose all the material items. The material items are the ones that influence the decisions of the financial statement users once they become aware of such items. I.e., omission or erroneous statement, could influence the economic decisions taken by the user, based on such financial statements

*The term 'accounting policies' in **AS 1** refer to the following while preparing financial statements an enterprise:*

- *specific accounting principles*
- *methods to apply those accounting principles*

Disclosure of Accounting Policies

- It is necessary to disclose all the significant accounting policies adopted while presenting & preparing financial statements.
- This is done to ensure proper understanding of financial statements.The disclosure of significant accounting policies should form part of the financial statements.
- An enterprise is free to change its accounting policies, unless it violates any statutory provisions, or codes laid down in a mandatory Accounting Standard, and provided of course such a change leads to better and more meaningful presentation of accounting information. If, however, such a change may have a material effect on the financial statements of the current accounting period or later periods, such changes should be disclosed.