01-C4: Generally Accepted Accounting Principles

Generally Accepted Accounting Principles (GAAP)

Financial accounting is governed by concepts and rules known as **generally accepted accounting principles (GAAP).** GAAP aims to make information *relevant, reliable,* and *comparable*.

Reliable information is trusted by users.

Relevant information affects decisions of users.

Comparable information is helpful in contrasting organizations.

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International Standards

In today's global economy, there is increased demand by external users for comparability in accounting reports. This demand often arises when companies wish to raise money from lenders and investors in different countries.

International Accounting Standards Board (IASB)	International Financial Reporting Standards (IFRS)
An independent group (consisting of individuals from many countries), issues International Financial Reporting Standards (IFRS)	Identify preferred accounting practices

Differences between U.S. GAAP and IFRS are decreasing as the FASB and IASB pursue a *convergence* process aimed to achieve a single set of accounting standards for global use.

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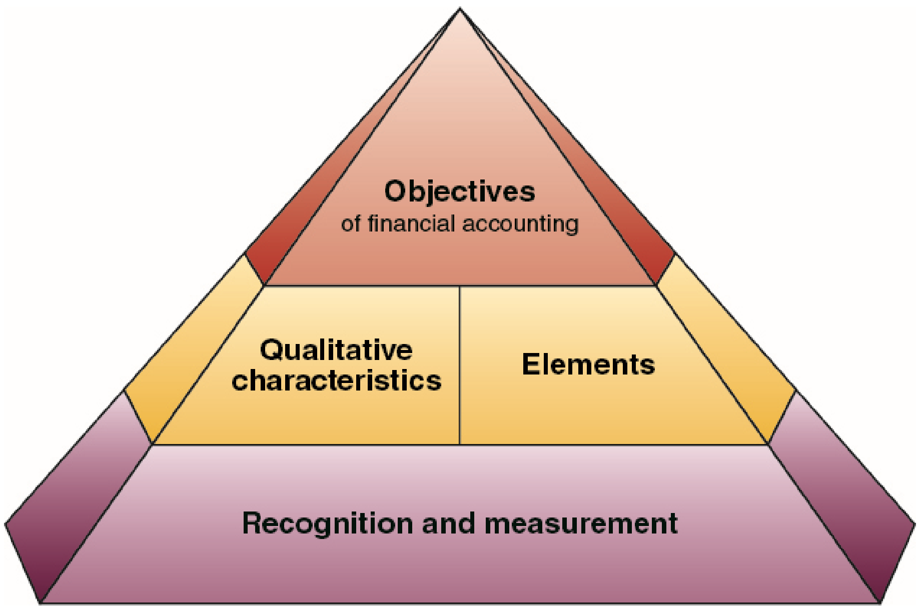
Conceptual Framework and Convergence

The FASB and IASB are attempting to converge and enhance the **conceptual framework** that guides standard setting. The framework consists broadly of the following:

- **Objectives**—to provide information useful to investors, creditors, and others.
- **Qualitative Characteristics**—to require information that is relevant, reliable, and comparable.
- **Elements**—to define items that financial statements can contain.
- **Recognition and Measurement**—to set criteria that an item must meet for it to be recognized as an element; and how to measure that element.



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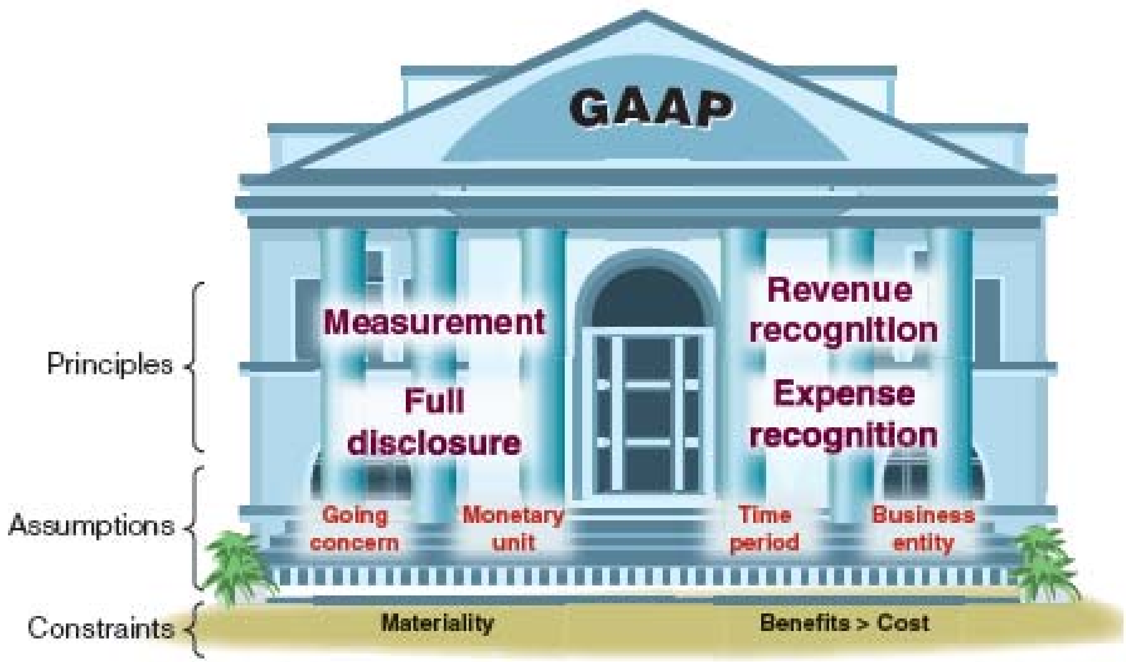
Principles and Assumptions of Accounting



General principles are the basic assumptions, concepts, and guidelines for preparing financial statements. General principles stem from long-used accounting practices.

Specific principles are detailed rules used in reporting business transactions and events. Specific principles arise more often from the rulings of authoritative groups.

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Accounting Principles

Measurement Principle (or Cost Principle)
Accounting information is based on actual cost. Actual cost is considered objective.

Revenue Recognition Principle
1. Recognize revenue when it is earned.
2. Proceeds need not be in cash.
3. Measure revenue by cash received plus cash value of items received.

Expense Recognition Principle (or Matching Principle)
A company must record its expenses incurred to generate the revenue reported.

Full Disclosure Principle
A company is required to report the details behind financial statements that would impact users' decisions.

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Accounting Assumptions

Going-Concern Assumption
Reflects assumption that the business will continue operating instead of being closed or sold.

Monetary Unit Assumption
Express transactions and events in monetary, or money, units.

Business Entity Assumption
A business is accounted for separately from other business entities, including its owner.

Time Period Assumption
Presumes that the life of a company can be divided into time periods, such as months and years.

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