

**MCM-505**

**ACCOUNTING THEORY & PRACTICES**

**UNIT-2 ACCOUNTING METHODOLOGY AND  
ACCOUNTING AS AN INFORMATION SYSTEM  
(M. COM. SECOND SEMESTER)**



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# Accounting Methodology

- There are the following two methodologies in accounting theory:-

- 1) Positive methodology

- Normative methodology

# Accounting as an Information System

- The term 'system' may be defined a set of elements which operates together in order to attempt a goal. Accounting comprises as series of activities linked together among them. The accounting activities form a progression of steps, beginning with observing, then collecting, recording, analyzing and finally communicating information to its users.

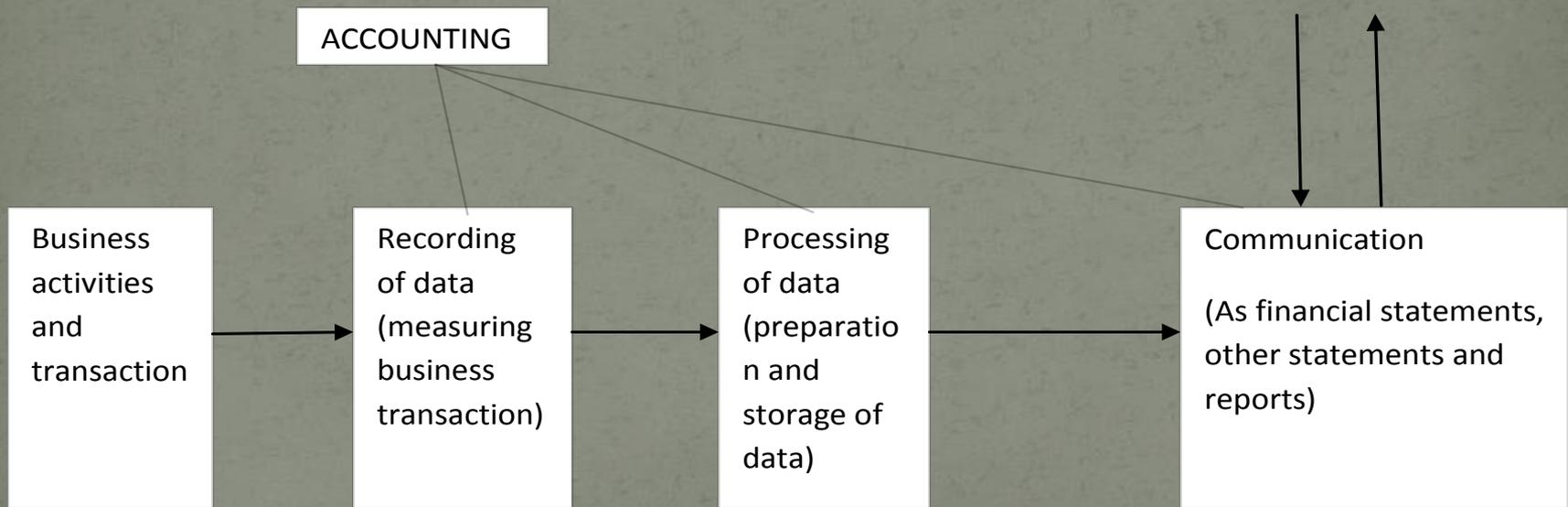
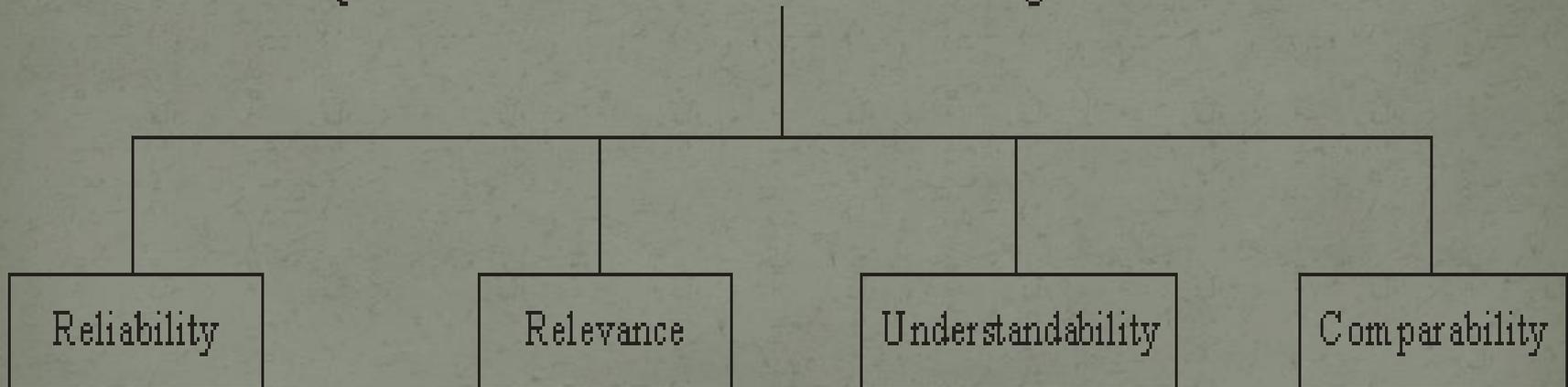


Figure: Accounting as an information in business decision

# Qualitative Characteristics of Accounting Information

- Qualitative characteristics are the attributes that make the information provided in financial statements useful to users. The four principal qualitative characteristics are:

## Qualitative Characteristics of Accounting Information



## **Constraints on Relevant and Reliable Information**

- The four constraints on relevant and reliable information are as follows:
  - **(i) Timeliness**
  - **ii) Balance between Benefit and Cost**
  - **(iii) Balance between Qualitative Characteristics**
  - **(iv) True and Fair View/Fair Presentation**

# **Types of Accounting Information**

- 1. Accounting Information relating to financial transactions and events**
- 2. Accounting information relating to cost of a product, operation or function.**
- 3. Accounting information relating to planning and controlling the activities of enter-prise for internal reporting**
- 4. Accounting information relating to Social Effects of business decisions.**
- 5. Accounting information relating to Environment and Ecology.**
- 6. Accounting information relating to Human Resources**

# Users of An Accounting Information and Their Needs

<i>Users</i>	<i>Need for Information</i>
<b>Short-term Creditors</b> [For example, suppliers of raw-materials/goods, suppliers of short-term loans]	Short-term creditors need information to determine whether the amount owing to them will be paid when due and whether they should extend, maintain or restrict the flow of credit to an individual enterprise.
<b>Long-term Creditors</b> [For example, suppliers of long-term loans]	Long-term creditors need information to determine whether their principals and the interest thereof will be paid when due and whether they should extend, maintain or restrict the flow of credit to an enterprise.
<b>Present Investors</b> [For example, equity share holders]	Present investors need information to judge prospects for their investment and to determine whether they should buy, hold or sell the shares.
<b>Potential Investors</b> [For example, those who want to invest]	Potential investors need information to judge prospects of an enterprise and to determine whether they should buy the shares.
<b>Management</b>	Management needs information to review the firm's (a) short term solvency, (b) long-term solvency, (c) activity ( <i>viz.</i> effective utilisation of its resources), (d) profitability in relation to turnover, (e) profitability in relation to investments and to decide upon the course of action to be taken in future.
<b>Employees</b>	Employees and their representative groups are interested in information about the stability and profitability of the employers. They are also interested in information which enables them to assess the ability of the enterprise to pay remuneration, retirement benefits and to provide employment opportunities.
<b>Tax Authorities</b>	Tax authorities need information to assess the tax liabilities of an enterprise.
<b>Customers</b>	Customers have an interest in information about the continuation of an enterprise, especially when they have established a long term involvement with, or are dependent on, the enterprise.
<b>Government and their agencies</b>	Government and their agencies are interested in the allocation of resources and, therefore, the activities of enterprise. They also require information in order to regulate the activities of enterprise, determine taxation policies and as the basis for the national income and similar statistics.
<b>Public</b>	Enterprises affect members of the public in a variety of ways. For example, enterprises may make a substantial contribution to the local economy in many ways including the number of people, they employ and their patronage of local suppliers. Financial statements may assist the public by providing information about trends and recent developments in the prosperity of the enterprise and the range of its activities. While all the information needs of these users cannot be made by financial statements, there are some needs which are common to all users. The information contents of the financial statements which meet information needs of the investors or providers of risk capital will also meet most of the needs of other users.

# Summary

- Accounting comprises as series of activities linked together among them. The accounting activities form a progression of steps, beginning with observing, then collecting, recording, analyzing and finally communicating information to its users. As an information system, accounting links and information sources or transmitter (generally the accountant), a channel of communication (generally the financial statement) and set of receivers (external users). When accounting is looked upon as a process of communication, it is define as “the process of encoding observations in the language of the accounting system, of manipulating the signs and statements of the systems and decoding and transmitting the results”
- Alternatively sometimes, the proceed data are further proceeds are prepared to provide useful information to users. The proceed and prepared information is communicated to users and decisions maker in the form of financial statements, other statements, report etc. In this accounting system the business transaction and activities are the input and statements and report given to decision makers are the output.

# References

- SILM developed by Uttarakhand Open University for MCM-505 (Accounting Theory and Practices), Year 2017,