Accounting Standards

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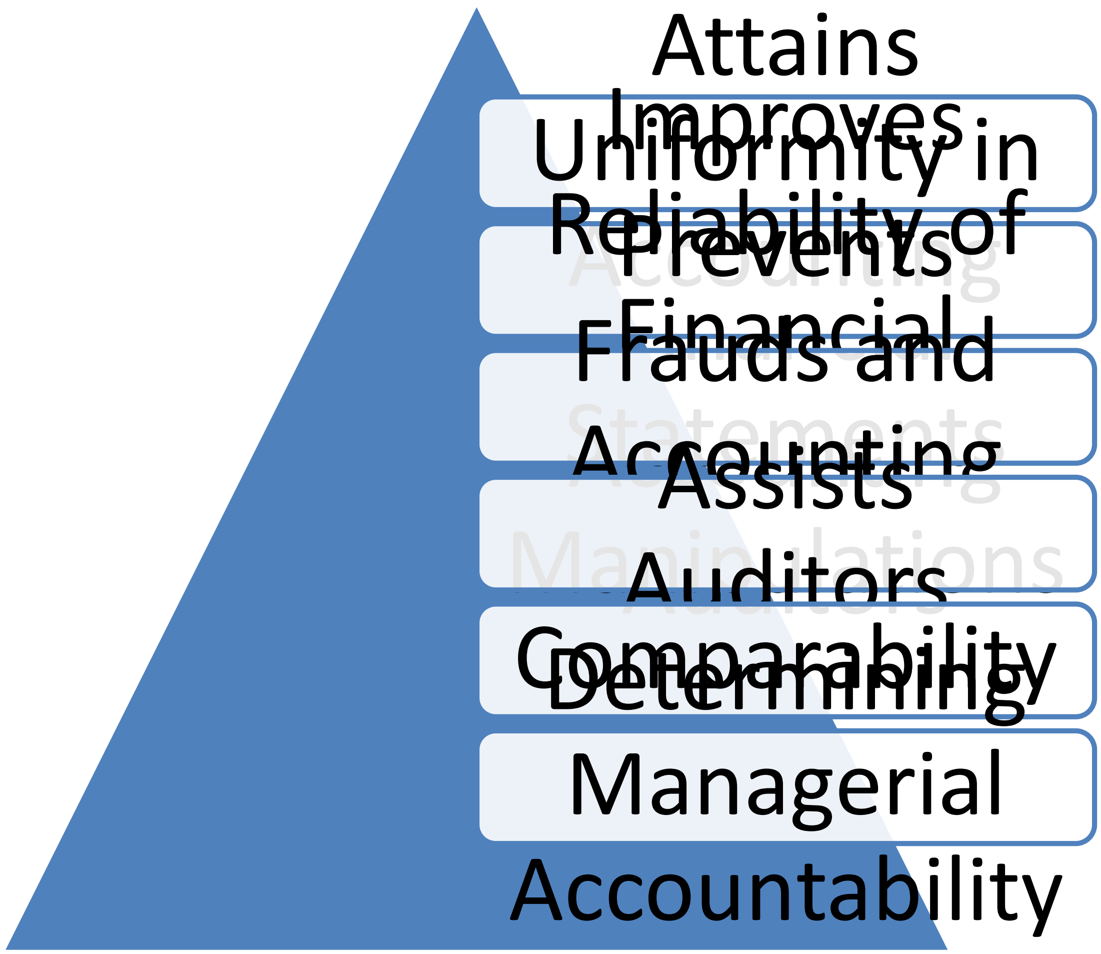
Accounting Standards

- Accounting Standards are written policy documents issued by expert accounting body or by the government or other regulatory body covering the aspects of recognition, measurement, treatment, presentation, and disclosure of accounting transactions in financial statements.

Objectives of Accounting Standards

- The main aim is to improve the reliability of financial statements. Now because the financial statements have to be made following the standards the users can rely on them. They know that not conforming to these standards can have serious consequences for the companies.
- Then there is comparability. Following these standards will allow for inter-firm and intra-firm comparisons. This allows us to check the progress of the firm and its position in the market.
- It also looks to provide one set of accounting policies that include the necessary disclosure requirements and the valuation methods of various financial transactions.

Benefits


Attains Uniformity in Accounting
Improves Reliability of Financial Statements
Prevents Frauds and Accounting Manipulations
Assists Auditors
Comparability
Determining Managerial Accountability

Benefits of Accounting Standards

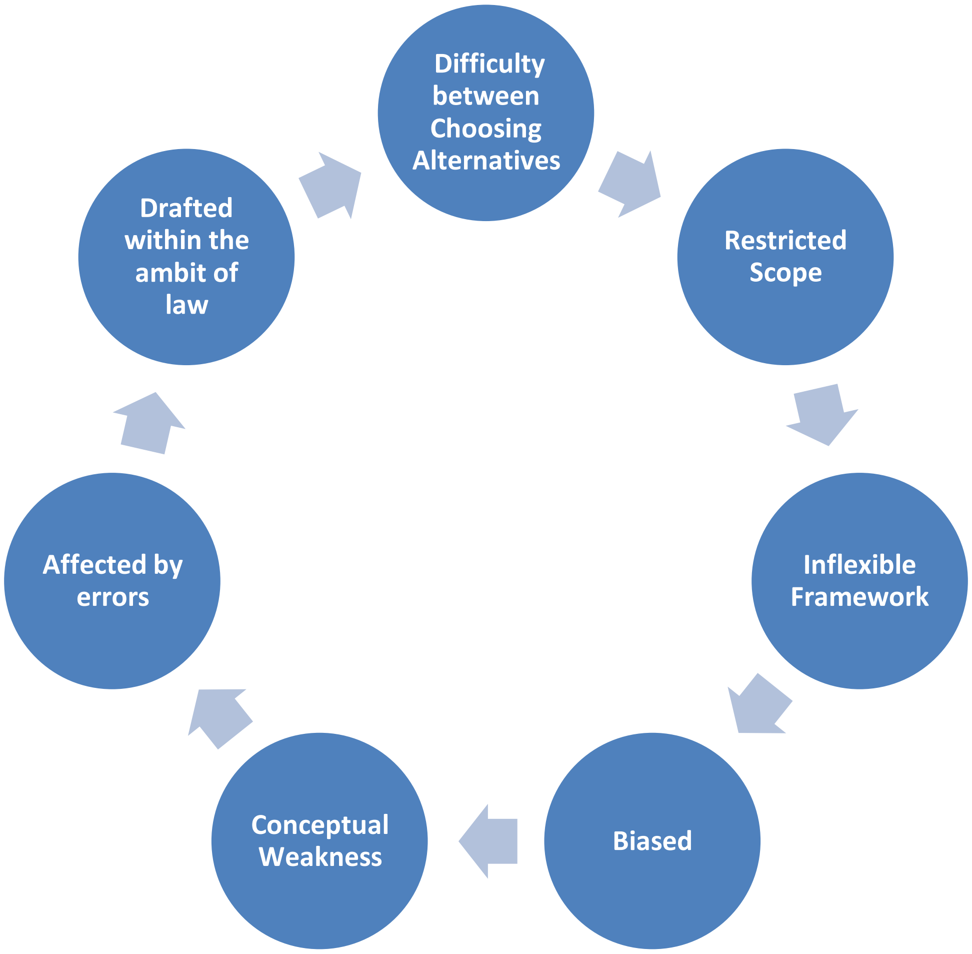
- **Attains Uniformity in Accounting**
- Accounting Standards provides rules for standard treatment and recording of transactions. They even have a standard format for financial statements. These are steps in achieving uniformity in accounting methods.
- **Improves Reliability of Financial Statements**
- There are many stakeholders of a company and they rely on the financial statements for their information. Many of these stakeholders base their decisions on the data provided by these financial statements.

- **Prevents Frauds and Accounting Manipulations**
- Accounting Standards (AS) lay down the accounting principles and methodologies that all entities must follow. One outcome of this is that the management of an entity cannot manipulate with financial data. Following these standards is not optional, it is compulsory.
- So these standards make it difficult for the management to misrepresent any financial information. It even makes it harder for them to commit any frauds.

- **Assists Auditors**
- Now the accounting standards lay down all the accounting policies, rules, regulations, etc in a written format. These policies have to be followed. So if an auditor checks that the policies have been correctly followed he can be assured that the financial statements are true and fair.
- **Comparability**
- This is another major objective of accounting standards. Since all entities of the country follow the same set of standards their financial accounts become comparable to some extent. The users of the financial statements can analyze and compare the financial performances of various companies before taking any decisions.

- **Determining Managerial Accountability**
- The accounting standards help measure the performance of the management of an entity. It can help measure the management's ability to increase profitability, maintain the solvency of the firm, and other such important financial duties of the management. Management also must wisely choose their accounting policies. Constant changes in the accounting policies lead to confusion for the user of these financial statements.

Limitations



Limitations of Accounting Standards

- **Difficulty between Choosing Alternatives**
- There are alternatives for certain accounting treatments or valuations. Like for example, stocks can be valued by LIFO, FIFO, weighted average method, etc. So choosing between these alternatives is a tough decision for the management. The AS does not provide guidelines for the appropriate choice.
- **Restricted Scope**
- Accounting Standards cannot override the laws or the statutes. They have to be framed within the confines of the laws prevailing at the time. That can limit their scope to provide the best policies for the situation.

- **Inflexible Framework:** An accountant has to follow that method only which is mentioned in the accounting standards while preparing accounts. It is not necessary that a method appropriate in one situation would be applicable in other situations as well.
- **Biased:** Accounting standards may be subject to lobbying or government pressure. Thus, in order to give unfair advantages to big corporate houses, the standards might be compromised.

- **Conceptual Weakness:** Earlier standards were not based on a sound conceptual framework of accounting but the ICAI is committed to rectify these.
- **Affected by errors:** They have been developed by human beings. So, there can be a chance of errors while developing these standards.
- **Drafted within the ambit of law:** They must adhere to the law of the country. It cannot go beyond the boundaries prescribed by the law of the country.

Need for Accounting Standards

- Accounting Standards are required to ensure the compliance of the following information with the qualitative characteristics of accounting:
- Profit or Loss of the business enterprise
- Financial Position of the business enterprise
- Inflow and outflow of Cash
- All the above information must suit the qualitative characteristics of accounting i.e. Reliability; Relevance; Understandability; and Comparability. Accounting Standards also assure its various users about the truth and fairness of the information contained in the Financial Statements of the business enterprise.

Uses of Accounting Standards

- They provide a standardized format that is to be followed while preparation of accounts, minimizing the variations in the method of preparation of accounts.
- They provide the basic rules on the basis of which financial statements are prepared.
- They make it compulsory for the businesses to form disclosure of the accounting policies followed while preparation of monetary statements.
- When a corporation complies with the accounting standards while preparation of monetary statements it creates a way of confidence among the users of monetary statements.

SCOPE OF ACCOUNTING STANDARDS

- **Standardisation of alternative accounting treatments -** accounting standards helps to reduce or eliminate upto a reasonable extent, any confusing variations in the accounting treatment and its presentation.
- **Requirements for additional disclosure -** there are certain areas where information is Statutorily required to be disclosed in addition, which make financial statements more reliable.
- **Comparability of financial statements -** it helps in the comparability of both intra and inter enterprises as it eliminates unnecessary accounting treatment alternatives.
  - **Intra enterprise comparison -** when compare the financial statements of same enterprise over a number of years.
  - **Inter enterprise comparison -** when compare the financial statements of different enterprises for same accounting period.

Thanks