FINANCIAL ACCOUNTING (ACC 1106)

BACHELOR OF PROCUREMENT AND SUPPLY CHAIN MANAGEMENT (BPSM)

Brendah Akankunda, PhD

bakankunda@mubs.ac.ug

+256772032695

LESSION ONE (1).

Topic One: The reporting framework of accounting in Uganda

1.1 Definition of accounting, types of accounting, role of accounting
1.2 . The regulatory system for accounting in Uganda
1.3 The framework for the preparation of financial statements

1.1.1 Definition of accounting

Accounting:

The process of identifying, measuring, recording, and communicating financial information about an entity to permit informed judgments and decisions by users of that information.

It is a service function; it provides financial information to the users.

Accounting encompasses various activities, including bookkeeping, financial reporting, auditing, and financial analysis,

It is essential for maintaining accurate records of financial transactions and ensuring the transparency and reliability of financial information provided to stakeholders.

QUIZ One (1)

……………is the process that involves identifying, measuring, recording, and communicating financial information about an entity, enabling users to make informed judgments and decisions?

A) Financial Reporting
B) Auditing
C) Budgeting
D) Accounting

1.1.2 Roles of Accounting

The objective of the general purpose of financial reporting:

- To provide financial information that is useful to users in making decisions relating to providing resources to the entity.

Users' decisions involve decisions about buying, selling, holding equity or debt instruments, providing or settling loans and other forms of credit and voting, or otherwise influencing management's actions.

Other Key Roles:

- Compliance and Regulatory Adherence.
- Decision-Making Support.
- Investment and Credit Assessment
- Taxation Purposes
- Communication with Stakeholders
- Performance Evaluation
- Historical Record Keeping

ASSIGNMENT ONE (1)

i. Explain the role of accounting in business operations and decision-making processes.

(10 Marks)

ii. How does accounting play a critical role in supporting and enhancing Procurement and supply chain activities within an organization?

(10 marks)

Instructions:

- **Submission Format:** Handwritten on 2 pages.
- **Group Work:** Complete this task as a group of 10 members.
- **Submission Deadline:** Submit by Noon on Thursday, 22nd.
- **Responsible Party:** Course leaders are responsible for submission.

1.1.3 Two Useful Classifications Of Accounting

1) **Operational accounting**: concerned with the use of accounting information for decision making by managers and investors.

1) **Equity accounting**: focuses on safeguarding and settlement of the economic rights and obligations of different groups of interest. ESG.

1.1.3.1 Types of Accounting

Types of Accounting	Definition
Financial Accounting	is the art and science of recording, classifying, summarizing, and communicating financial transactions and information through financial statements, and interpreting the results to aid decision-making.
Cost accounting	This is a tool of management that provides a detailed record of the costs relating to products, services, operations or activities. It is a process of determining and accumulating the cost of some particular product or service.
Management Accounting	The application of accounting techniques for providing information designed to help all levels of management in planning and controlling the activities of a business enterprise and in decision
Environmental Accounting	Refers to an approach taken by organizations to track the effects of their actions on the environment. It incorporates environmental conservation and management principles into cost-benefit analyses and reporting practices.
Social Accounting	It is a process of evaluating a company's impact on society and the environment alongside its financial performance.
National Accounting:	This analyzes a country's economic activities, examining expenditures and returns, project efficiency, and public sector management.

Operational

Equity

1.1.4 Differences between financial accounting and management accounting

Basis	Financial Accounting	Cost / Management Accounting
• level of regulation	Highly regulated	Non-Regulated
• Need for audit	The audit is a requirement	No need for auditing
• Reporting format	Specified formats as stipulated in the law and Accounting standards	No specific format
• Reporting frequency	Annually	Routine reporting eg daily, weekly etc
• Level detail	Summarized	Detailed
• Nature of data	Financial	Financial and non-financial
• Focus	Historical data and past financial performance.	Future projections, budgeting, and cost control.
• Users	Mainly for External users like investors, creditors, regulators, and tax authorities.	Mainly for Internal users such as managers and executives.

1.2 . The regulatory system for accounting in Uganda

1.2.1 The need for regulation of accounting.

1.2.2 Forms of Regulation.

1.2.3 Accounting standards – their purpose, the standard-setting process, and the role of the ICPA and the IASB.

1.2.1 The Accounting Standards/Regulations

- Accounting standards are a set of guidelines and rules that define how financial transactions should be recorded and reported.

- Accounting standards are a set of guidelines and rules that are used to govern the preparation and presentation of financial statements.

- These standards are necessary to ensure that financial statements are accurate, transparent, and comparable.

- These standards provide a common language for financial reporting, which makes it easier for investors and creditors to compare the financial performance of different companies.

1.2.2 The Need for / Role of Accounting Standards in Financial Reporting

- To ensure that financial statements are accurate, transparent, and comparable.
- To provide a framework for financial reporting that is consistent across different companies and industries (reports are prepared in a standardized and consistent manner).
- To promote transparency, accountability, and comparability in financial reporting.
- To enable stakeholders to make informed decisions about a company’s financial health and prospects.
- To ensure the full disclosure principle which requires companies to disclose all relevant information about their financial position, including any potential risks or uncertainties.
- To ensure that stakeholders have access to all the information they need to make informed decisions about a company’s financial health and prospects.
- To ensure that financial statements are audited by independent auditors, providing investors with additional assurance that the financial statements are accurate and reliable.

1.2.3 Accounting Standards' Bodies.

- Accounting standards are developed by various bodies, including the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB).

- These bodies work to establish generally accepted accounting principles (GAAP) that are used by companies around the world.

- **International Financial Reporting Standards (IFRS)** are a set of accounting standards that are used in many countries around the world. They are developed by the IASB and are designed to provide a common language for financial reporting.

- **The IASB** is an independent organization that is responsible for developing and promoting the use of IFRS. It works to develop accounting standards that are used by companies around the world.

- **National/local legislation** like constitution, and company's act: Limited liability companies are required by law to prepare and publish accounts annually as per national legislation.

1.2.4 The role of the Institute of Certified Public Accountants (ICPA)

- ICPAU membership comprises professional accountants and auditors.

✓Setting and maintaining accounting and auditing standards

✓Setting licensing requirements for accounting firms, and issuing and renewing licenses Issuing practicing certificates to qualified members who wish to practice accountancy;

✓ Maintaining a register of practicing accountants;

✓Setting initial professional development and continuing professional development requirements and regulating practical training;

✓Establishing ethical requirements;

✓Monitoring the conduct and performance of its members, including quality assurance reviews

✓Investigating and disciplining members for misconduct and breach of professional standards; and

✓ Advising the government on matters of financial accountability.

1.2.5 Different forms of financial reporting regulation

- **The Companies Act (Cap 110)** - legislation governs the formation, management, and dissolution of companies in Uganda, and legal requirements for financial reporting.
- **Accounting standards-** formal guidelines and rules that govern companies' accounting and financial reporting practices.
- **The Capital Markets Authority**. The regulatory body is responsible for overseeing the capital markets in Uganda.
- **The Uganda Securities Exchange**. Enforces financial reporting requirements for companies that are listed on the exchange.
- **Financial Institutions Act** (Cap 54). Regulates financial institutions in Uganda.
- **Insurance Act** (Cap 213). Sets out the financial reporting obligations for insurance companies
- **The National Environment Act, 2019**; companies are required to conduct environmental audits and submit compliance reports to NEMA.
- **The Public Finance Management Act, 2015;** for fiscal and macroeconomic management of Public entities in Uganda.

1.2.6 The standard-setting process

The due process for developing an IFRS comprises six stages:

1. Setting the agenda- identifies a need for a new standard or an amendment to an existing standard

2. Planning the project –IASB consults with stakeholders and sets a timeline for the development of the new standard or amendment

3. Development and publication of Discussion Paper - to gather input on the need for changes.

4. Development and publication of Exposure Draft - seeking feedback from the public, including companies, auditors, and other stakeholders.

5. Development and publication of an IFRS Standard-After considering feedback from the Exposure Draft, the IASB is finalized and issued.

6. Procedures after a Standard is issued- IASB provides implementation support, monitors how the standard is applied globally, and may issue amendments or additional guidance based on practitioner feedback.

1.3 The framework for the preparation of financial statements

- The main financial statements and their purpose
- Users of accounting information and their information needs
- Accounting concepts – going concern, accruals, consistency, materiality, substance over form & prudence.
- Qualitative characteristics of financial statements – relevance, reliability, comparability & understandability.
- Elements of financial statements – definitions of assets, liabilities, equity, revenue, and expenses; Measurement of the elements – historical cost, replacement cost, net realizable value & economic value

1.6.1 Users of financial statements and their needs

Accounting information helps a variety of users to make better financial decisions.

Users of financial information may be both internal and external to the organization.

Accounting information is presented to internal users usually in the form of management accounts, budgets, forecasts, and financial statements.

1. **Internal users** (**Primary Users**) of accounting information include the following:

- **Management:** for analyzing the organization's performance and position and taking appropriate measures to improve the company results.
- **Employees**: for assessing the company's profitability and its consequence on their future remuneration and job security, potential bonuses or raises.
- **Owners**: for analyzing the viability and profitability of their investment and determining any future course of action.

1.6.2 Users of financial statements and their needs.

2.1 External users (**Secondary Users**) of accounting information:

- **Creditors**: for determining the creditworthiness of the organization. Terms of credit are set by creditors according to the assessment of their customers' financial health.
- **Tax Authorities**: for determining the credibility of the tax returns filed on behalf of the company.
- **Investors**: for analyzing the feasibility of investing in the company.
- **Customers**: for assessing the financial position of its suppliers which is necessary for them to maintain a stable source of supply in the long term.
- **Regulatory Authorities**: for ensuring that the company's disclosure of accounting information is by the rules and regulations set to protect the stakeholders' interests in forming their decisions.

2.2 External users (Secondary Users)

- **The Government and its agencies** are interested in the allocation of resources and, the activities of entities. They also require information to regulate entities' activities, determine taxation policies and as the basis for national income and similar statistics.
- **The Public**, Financial statements may assist the public by providing information about the trends and recent developments in the prosperity of the entity and the range of its activities.
- **Financial Analysts**: Investment analysts are an important user group - specifically for companies quoted on a stock exchange.
- **Trade Unions**: Wage negotiations, job security and employee welfare.
- **Professional Institutions**: Standards Compliance, Membership Dues and Professional Development.

1.6.3 MAJOR USERS: Investors And Creditors

Which aspects of financial accounting information do investors and creditors evaluate when making investment and credit decisions?

- Profitability. Incomes vs expenses.
- Liquidity: the ability to pay current obligations.
- Solvency: whether the business has enough resources to pay its debts.
- Stability: Does the business have enough control over debt, do sales revenues confirm market demand for the products?
- Growth: new products, new technologies.

Information is provided for users to make their evaluations, estimates, and predictions.

Quiz Three (3)

1) How do various individuals and groups within and outside the organization utilize accounting information for decision-making?
   - ✓ Provide a table to illustrate the users and their specific information needs.

(select any Manufacturing company of your choice and illustrate this).

(10 marks)

2) How does accounting play a critical role in supporting and enhancing Procurement and supply chain activities within an organization?

(10 marks)

1.6 Types/Forms of business entity

"Entity" means a single separate body or organization.

Businesses of whatever size or nature exist to make a profit.

Profit is the excess of income over expenditure.

Ways of looking at a business:

A business as a **commercial or industrial concern** that exists to deal in the manufacture, resale, or supply of goods or services.

A business is an **organization that uses economic resources** to create goods or services that customers will buy.

A business is an **organization providing jobs** for people.

A business invests **money in resources** (for building, machinery, employees) to make even more money for its owners.

There are three types of business entities/organizations which include;

- Sole proprietors
- Partnerships
- Limited liability companies

Items	Sole proprietorships	Partnerships	Limited liability companies
Definition	A business owned and run by one individual, perhaps employing one or two assistants and controlling their work	It occurs when two or more people decide to run a business together with a common view to making a profit. Partnerships are generally formed by contract (Partnership agreements/deed)-capital, profits, responsibilities, salaries, procedures dissolving the partnership.	Limited liability companies are incorporated to take advantage of "limited liability" for their owners (shareholders). the shareholders of a limited liability company are only responsible for the amount paid for their shares. A limited liability company is legally separate from its owners or shareholders.
Examples	Shopkeeper, a plumber, boutique, hairdresser	Accountancy practice is a medical and legal practice.	Private limited companies, Public limited company, Companies limited by Guarantee (Football clubs; NGOs)
Assumptions	• Single ownership • One person control. • Unlimited liability. • Earns the profits or stands for the loss of the venture.	• The minimum number of members in a partnership is 2 -20. • It may be a group of individuals/companies owning one business and who contribute capital. • They have unlimited joint and several liabilities for each member. • There is no perpetual/continuous succession • The main objective is profit for the partners. • Partners are governed and guided by a partnership deed • Profits and losses are shared basing on the agreed terms	• It is limited by shares • Minimum number of members is 7 and it has no maximum • It can offer its shares and debentures to the public to subscribe. • Its shares are transferable without any restrictions. • It has to hold a statutory meeting and file a statutory report.
Reporting	A sole trader must maintain accurate financial records and produce financial statements that can be used to calculate taxes, and support applications for loans and overdraft facilities	Partnerships must maintain financial records and produce financial accounts.	Limited liability companies have to publish annual financial statements to the public.
Merits	✓ The owner has complete control over the business. ✓ Owner is entitled to all the profits and the ownership of the assets ✓ Can be highly flexible ✓ Less stringent reporting obligations ✓ It does not require much capital to start.	✓ Less stringent reporting obligations ✓ Additional capital can be raised by admitting new partners ✓ Division of roles and responsibilities and an increased skill set. ✓ Sharing of risks and losses between more people. ✓ No company tax on the business (profits are distributed to partners and then subject to personal tax) ✓ Formation is fairly simple	✓ Can easily raise capital through issue of shares. ✓ Owner's liability for debts of the company is limited to the share capital contributed. ✓ Company has a separate legal entity from its owners. ✓ It is relatively easy to transfer shares from one owner to another. ✓ Tax advantages to being a limited liability company. ✓ Can employ experts, be more efficient and enjoy economies of scale.
Demerits	✓ Unlimited liability ✓ Personal property may be vulnerable to debts and other business liabilities. ✓ Capital resources are limited which limits the expansion of the business ✓ Difficulties in business continuity in the event of death or illness of the owner. ✓ Poor decision making	✓ Partners are jointly liable for all debts (unlimited liability)- unless they have formed a limited liability partnership. ✓ Costs associated with setting up partnership agreements. ✓ Difficulties in continuity of the business in the event of death or illness ✓ Slower decision making due to the need for consensus ✓ Profits are shared, which reduces the amount received by each partner.	✓ Stringent reporting obligations inline with the requirements. ✓ Auditing requirements ✓ Share issues are regulated by law. ✓ Delays in decision making.

Quiz Two (2)

Discuss Five (5) differentiating features between:

a) a partnership and a limited company.
b) A sole proprietorship and partnership
c) Private limited companies and Public limited company
d) Partnership and Companies limited by Guarantee

1.6 The Accountant

An “accountant” means a person who is enrolled as a member of the Institute in accordance with the Act;

What Roles Do Professional Accountants perform in Business?

The roles professional accountants perform can be described as creators, enablers, preservers, and reporters of sustainable value for their organizations in both performance and conformance dimensions:

Ability to recognize valid data, make required inputs, perform functional manipulations, generate reports, and interpret results.

the Fundamental ethical principles for professional accountants (Code of ethics)

Integrity: A professional accountant should be straightforward and honest in all professional and business relationships

---

Objectivity: A professional accountant should not allow bias, conflict of interest or undue influence of others.

Professional Competence and Due Care: A professional accountant has a continuing duty to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional services based on current developments in practice, legislation and techniques. A professional accountant should act diligently and by applicable technical and professional standards when providing professional services.

Confidentiality: A professional accountant should respect the confidentiality of information acquired as a result of professional and business relationships and should not disclose any such information to third parties without proper and specific authority unless there is a legal or professional right or duty to disclose.

Professional Behavior: A professional accountant should comply with the relevant laws and regulations and should avoid any action that discredits the profession.

1.6 REPORTING FRAMEWORK OF ACCOUNTING IN UGANDA

A) The Regulatory Frame Work

- **National/local legislation :** In most countries, limited liability companies are required by law to prepare and publish accounts annually.
- **GAAP (Generally Accepted Accounting Principles)**: A general term for a set of financial accounting standards and reporting guidelines used to prepare accounts in a given environment.
- **International Financial Reporting Standards Foundation (IFRS)** Responsible for governance of standard setting process.
- In March 2018, the International Accounting Standards Board (the Board) revised the Conceptual Framework for Financial Reporting (the Conceptual Framework

1.6 Different Forms Of Financial Reporting Regulation

The Companies Act (Cap 110)

Accounting standards.

The Capital markets Authority

The Uganda Securities Exchange.

Financial Institutions Act (Cap 54) Insurance Act (Cap 213)

Institute of certified public Accountants (ICPAU)

ACCOUNTING CONCEPTS/PRINCIPLES/ASSUMPTIONS

- Accounting concepts also known as principles, conventions, or postulates are basic ground rules that must be followed when financial accounts are being prepared and presented.
- They are also referred to as assumptions or prepositions that underlie the preparation and presentation of financial reports.

Accounting Concepts

Business Entity Concept. Ensure that private financial transactions and matters relating to the owner of a business is recorded and separated from financial transactions that relate to the business.

Monetary measurement / unit of measurement concept : All transactions to be recorded must be quantified in monetary terms, since money is a common denominator for all transactions e.g. cost, sales, the value of stocks, machinery, debts and investments.

Going Concern/ continuity: The accounting records to be maintained in such a way that the business is seen to continue in its foreseeable future. the financial reports are prepared with the expectation that a business will remain in operation indefinitely.

Periodicity: This requires a company to prepare and disclose financial reports at the end of every accounting or financial year.

Historical cost: This principle requires transactions to be recorded at the price ruling at the time, and for assets to be valued at their original cost. That is, the actual amount paid for items bought is recorded.

Accounting Concepts

Realization concept : This concept requires that transactions are recognized and recorded at the point of sale or transfer of legal ownership – rather than just when cash actually changes hands.

Materiality: This requires the recognition of only material items and excluding immaterial or trivial or significant items. Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial reports.

Consistency: Transactions and valuation methods are treated the same way from year to year, or period to period. Business decisions are often made by comparing current financial reports with previous financial reports.

Prudence/ conservatism: This concept requires the profits are not recognized until a sale has been completed. In addition, a cautious vie should be taken for future problems and costs of the business as soon as there is a reasonable chance that such costs will be incurred in the future i.e. provide for all possible losses, for example, provision for bad debts.

Accrual concept: This requires the recognition of items at the occurrence of the transaction and not when cash is received or paid. For example, Income is recorded as earned even though it might have not been received.

Matching. This concept requires that revenues from business activities and expenses associated with earning that revenue are recorded in the same accounting period.

Accounting Concepts

Substance over form: This states that transactions and other events should be recorded in accordance with financial and economic reality (substance) other than their legal form. E.g. in a hire purchase, the buyer takes possession and use of the asset but does not the buyer takes possession and use of the asset but does not become the legal owner until the last installment has been paid.

Duality concept (dual aspect): This is the basis of double entry book keeping and stems from the fact that every transaction has a double (dual) effect on the position of a business as recorded in the accounts.

ACCOUNTING CONCEPTS (RECAP)

Self Assessment: Multiple choice Questions

The assumption that an organisation will continue to operate indefinitely is a fair description of which concept?

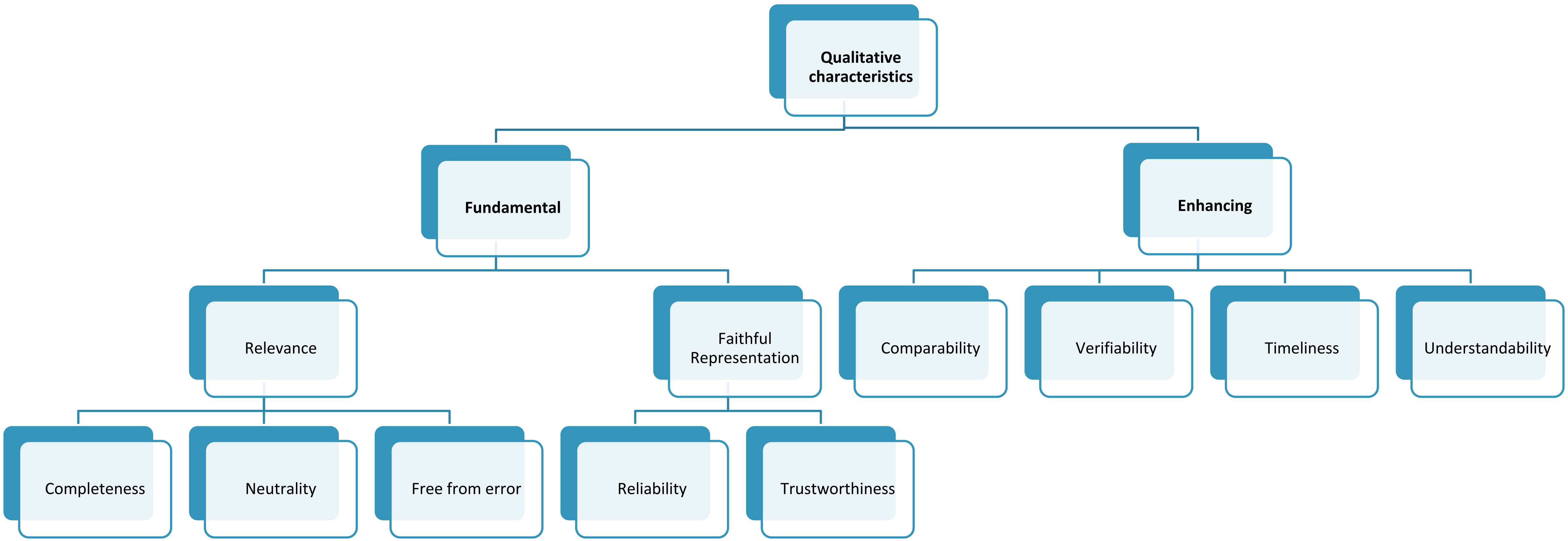
(a) Accruals
(b) Going concern
(c) Consistency
(d) Prudence

The concept of materiality implies that an organisation will:

(a) Only account for items which don't affect the overall view gained from its accounts.
(b) Not account for non-current assets which are due to be sold in the next accounting year.

1.7 Qualitative Characteristics Of Useful Financial Information

- The framework identifies fundamental and enhancing qualitative characteristics (Attributes of accounting information).



Fundamental qualitative characteristics

- **Relevance**: Relevant financial information is capable of making a difference in the decisions made by users. Information influences decisions if it has;
  - **predictive value** if it can be used by users to predict future outcomes.
  - **confirmatory value** if it provides feedback about previous evaluations so that it is used to confirm or correct past evaluations and assessments.
  - Both: The predictive value and confirmatory value of financial information are interrelated; one uses revenue information for the current year, as the basis for predicting revenues in future years.

- **Faithful representation:** Financial information is useful if it faithfully represents the economic aspects of an entity in words and numbers that it purports to represent. Information faithfully represents the entity if it is:
  - ✓ Transactions and events are accounted for by their substance and economic reality and not merely their legal form.
  - ✓ **Complete** – includes all necessary descriptions and explanations that is necessary for a user to understand the item like the nature and amount.
  - ✓ **Neutral** – the information is presented without bias and is not manipulated to be received favorably or unfavorably by users.
  - ✓ **Free from error** – means: There are no errors or omissions in the description of the item. The process used to produce the reported information has been selected and applied with no errors in the process.

Enhancing qualitative characteristics

- These enhance the usefulness of information that is relevant and faithfully represented.
- **Comparability** Information about a reporting entity is more useful if users can compare it with similar information: For earlier periods of the same business; Of other businesses for the same period; In the budget or forecast. Enables users to identify and understand similarities and differences among items.
- **Verifiability:** assure users that information faithfully represents the economic aspects it purports to represent. means that different knowledgeable and independent observers could reach a consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation.

e.g cash is verified by counting it

- **Timeliness** means having information available to decision-makers in time to be capable of influencing their decisions. Available when needed.
- **Understandability:** Classifying, characterizing, and presenting information clearly and concisely makes it understandable.

Self assessment

1. Which of the following best describes "Relevance" in financial information?

A) Information that is free from error.

B) Information that provides a complete picture of the financial status.

C) Information that is capable of making a difference in the decisions made by users.

D) Information that is neutral and unbiased.

2. What is "predictive value" in the context of financial information?

A) Information that can be used to confirm or correct past evaluations.

B) Information that helps users predict future outcomes.

C) Information that provides a complete description of an item.

D) Information that is presented without bias.

3. Which statement best describes "Faithful Representation"?

A) Information that helps users predict future outcomes.

B) Information that faithfully represents the economic aspects of an entity in words and numbers.

C) Information that is relevant to the decisions made by users.

D) Information that has predictive and confirmatory value.

4. Which of the following is NOT a component of Faithful Representation?

A) Completeness

B) Neutrality

C) Predictive value

D) Free from error