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The Building Blocks of Accounting : Ethics, Principles, and Assumptions

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Abstract

The accounting system is one of the information systems among various types of information systems used by management in managing the financial statements of a company. Each system consists of the building blocks that make up the system. Understanding the basic building blocks in accounting will make it easier to understand accounting concepts correctly.
The basic terms that must be understood in accounting, namely: Income, Expenses, Assets, Liabilities, Owner's Equity, Debits, and Credits. To fulfill the basic building blocks in accounting, it is also necessary to pay attention to elements in accounting records such as ethics, principles and assumptions used in the accounting process. By paying attention to the elements in the accounting records, it is possible to provide financial statements in accordance with the standards used in reporting financial statement.

Keyword : Accounting system, ethics, principles, assumptions

1. INTRODUCTION

This paper discusses the extensively explored Building Blocks of Accounting: Ethics, Principles, and Assumptions. Ethics is a belief system that allows us to differentiate right from wrong and identify good and bad behavior.You will certainly face ethical situations at school and will face similar situations at work. Companies must be able to identify ethical issues and analyze options, what is right and wrong and what should be do. Ethical decisions mean choosing the best available option under the conditions.

Financial accounting is governed by a set of rules called Financial Accounting Standards (SAK or GAAP) for short (Tiosanna et al., 2020). Generally accepted accounting principles (GAAP) identify three main characteristics of information, there are : First, information must be relevant. Relevant information affects the decisions of users for financial information. Second, the information must be reliable. Lastly, the information must be comparable. Comparability helps us compare financial information from one period to the next.

The Monetary Unit Assumption tells us that we only record accounting information that can be expressed in monetary units. Assumptions of an Economic Entity require that the activities of the entity be kept separate and different from those of its owners and all other economic activities entity. The Time Period Assumption states that the economic life of a business can be divided into artificial time periods (Putri, 2020). The assumed time period that begins on January 1 and ends on December 31 is called the calendar year. The Cost Principle tells us that accounting information is based on actual costs or as historical costs. The Objectivity Principle states that accounting information should be unbiased and based on independent evidence.
The Full Disclosure Principle states that financial statements report what sensible people need to know to make the right decisions. The Revenue Recognition Principle states that revenue should be recorded in the company's accounts when it is earned. The Matching Principle requires that expenses be recorded in the same period as the income they generate is recorded. If the application of accounting theory results in incompatible or inconsistent

statements, then industry practice should be examined for possible explanations.

2. LITERATURE RIVIEW

The concept of building Accounting is the Basic Accounting Equation, namely :

ASSETS = LIABILITIES + OWNER'S EQUITY

Accounting must apply the Basic Accounting Equation above any type of entity. In simple terms, the above equation explains that; The resources of an entity (Assets), will be claimed by the creditors (called Liabilities) and will also be claimed by owners (called Owner's Equity).

Accounting in a company must apply the basic concepts of accounting without exception, so that accounting can be carried out properly. The basic concepts of accounting are Ethics, Principles and Assumptions.

Ethics – Fundamental business concepts

Regardless of the type of work, one person's actions will have an impact on other people or other organizations (Doan et al., 2022). Of course, what we expect of everyone is to do what is right, honest and fair. Imagine when you want to run a business or want to invest, but it turns out that everyone around you is not an honest person. The standard of behavior that is the basis for judging whether someone is doing right or wrong, honest or dishonest, fair or unfair, is what is called Ethics. Same like Accounting, which of course does not escape the importance of applying Ethics. Therefore, ethics is a concept that must be applied so that all business actions must be ethical, legal and accountable. For this reason, Ethics is a fundamental business concept.

Generally accepted accounting principles

In order to avoid differences in perceptions and interpretations, it is necessary to make standards for how economic events are recorded and reported that are generally and universally accepted (Fachrizzu et al., 2020). Accounting principles must be compiled in an accounting standard that is generally accepted, not only for the organization, but also in a wider scope. Indonesia already has an accounting standard called SAK (Financial Accounting Standards). SAK has 4 variants, there are:

1. **PSAK-IFRS (Statement of Financial Accounting Standards – International Financial Report Standard)**
   This type of SAK is used by entities or businesses that have public accountability, registered entities or are in the process of registering in the capital market. And because Indonesia is a member of the International Federation of Accountants (IFAC), it must implement IFRS.
2. **SAK-ETAP (Financial Accounting Standards – Entities Without Public Accountability)**
   ETAP is the result of simplification from IFRS (International Financial Reporting Standard) (Lubis, 2020). The implementation of ETAP can enable small and medium-sized businesses to make financial reports without being assisted by other parties and allow them to have accountability.
3. **PSAK-Syariah**
   Applied to institutions that implement syariah policies because they were developed based on fatwas and MUI.
4. **SAP (Government Accounting Standards)**
   This standard is applied to government institutions in preparing financial reports, both LKPP (Central Government Financial Report) and LKPD (Local Government Financial Report).

There are 2 institutions that are responsible for accounting standardization in Indonesia, namely : First, The Financial Accounting Standards Board (DSAK) is under the auspices of the Indonesian Institute of Accountants (IAI) and the second is the Capital Market Supervisory Agency (BAPEPAM), a government agency. In general, both of them work together to ensure that the standards developed are timely and useful Accounting Principles.

An example of an important principle in accounting is the cost principle, which states that assets should be recorded at cost, the price at which they were acquired. The opposite of acquisition price is market price.

Assumption

Accounting must use 2 assumptions, namely the Money Unit Assumption and the Economic Entity Assumption in its application, so that it has accurate results.

Based on the Unit of Money Assumption, only transaction data that can be expressed in units of money are entered into accounting records. Because accounting records must be something that can be measured, this assumption is very important and must be applied.

Meanwhile, based on the Economic Entity Assumptions, it is stated that the activities of the entity must be separated and differentiated between the activities of the Owner and other economic activities. What is meant by Entity is whether it is an organization or a unit in the community, for example companies, governments, universities, houses of worship and others. Accounting must be applied by separating personal activities and activities of economic entities.

In terms of business, Indonesia recognizes 3 types of entities, there are:

1. **Sole Proprietorship**

   A company owned by one person. In general, the business owner is also the manager that manage the business itself. From a legal perspective, there is no separation of liability for business and personal assets, however, business accounting activities must be separated from personal financial records and owner activities.

2. **Guild Company**

   Basically the same as a sole proprietorship but has a difference in the number of owners, that is owned by 2 or more people in the form of a partnership. The owners make an agreement both verbally and in writing that regulates the terms and responsibilities of each partner. As with sole proprietorships, from a legal perspective, there is no separation of liability for business and personal assets, but business accounting activities must be separated from personal financial records and owner activities.

3. **Limited Liability Company**

   A company which is legally an independent entity separate from its owners. Company ownership is divided into shares which can be transferred or traded. The liability of the owner's property and the company is legally separate which automatically has separate accounting activities.

3. METHODS

In general, there are two accounting methods, namely cash basis and accrual basis. Both of them are often used because they relate to accounting principles. Among them are the principles of economic entities, the principles of accounting periods, and so on. The following describes the two accounting methods.

1. Cash Basis

Accounting records which are prepared on a cash basis, recognize income and expenses according to real-time cash flows. Income is recorded at the time the funds are received, not based on when they are actually earned. Expenses are recorded when they are paid, not when they are incurred.

Therefore, in this accounting method it is possible to defer taxable income by delaying collection, so that payments are not received in the current year. Likewise, it is possible to expedite expenses by paying them as soon as the bill is received, before the due date.

Benefit of cash basis method

- Cash basis accounting methods require relatively less effort and are easier to understand and report. Because it doesn't require a lot of accounting staff and in most cases, it can be handled on its own.

- Directly reflects the value of cash inflows and outflows, which helps understand current profitability in monetary terms.
- It allows recording only the actual receipts to be taxed, not the total income. This method can help companies in tax planning and avoid large tax burdens in periods of cash crunch (lower net inflows).
- Suitable for small businesses with no inventory or few assets, business start-ups, and individuals who generally prefer the cash method for easy accounting.

2. Accrual Basis

Companies that use the accrual basis for accounting, recognize revenues and expenses when they are earned or incurred, regardless of when the cash associated with the transaction changes hands. Under this system, revenue is recorded when an order is received rather than when payment is received. Expenses are recorded when incurred, not when payment is made.

Benefit of accrual basis method

- The accrual method provides a more accurate, clearer picture of the company's financial condition, in a certain accounting period.
- Most investors and analysts find financial statements reported using the accrual method to be more useful in measuring company performance.
- The accrual method also provides a stronger basis for estimating future income and expenses and for making related decisions.
- Usually large companies, bona fide, and public companies that use the accrual method that makes it easy to set certain criteria for companies that are required to do tax calculations.

4. RESULT AND DISCUSSION

4.1 RESULT

In accounting activities, we will go through various processes in it, sart from checking financial transactions to bookkeeping or preparing financial statements. Activities that are continuously repeated are called the accounting process.

Accounting records will make it easier to understand through the classification into groups such as Income, Expenses, Assets, Liabilities, Owner's Equity, Debits, Credits, and will be presented in the illustration below;

Income and Expenses

An income is a one-time transaction that gives you money. An income account looks something like this:

Income	
Sales Revenue from Product for the Month of 5 Dec 21	$2000
Sales Revenue from Services Provided for the Month of 9 Dec 21	$1000

An expense is a one-time transaction that takes money away from you. An expenses account looks something like this:

Expenses	
Payment of Utility Bills for the Month of 20 Dec 21	$500
Purchase of New Machinery 19 Dec 21	$1000

Assets and Liabilities

An asset is simply anything of value that you own. So, what constitutes value? Something is of value when it can be exchanged for money, or when it can generate money or contribute in some way to income. In other words, an asset is anything that contributes to income. An asset account looks something like this:

Assets	
Office Building 2 Dec 21	$300000
Office Furniture 3 Dec 21	$800

A liability is the opposite of an asset. It is anything that you own that takes money away from you. In other words, a liability is anything that you own that will cause you to incur an expense. A liability account looks like this:

Liabilities	
Money Payable to Supplier for 500 sheets of paper 26 Dec 21	$2000
Monthly Wages Payable to Employees 30 Dec 21	$1000

Owner's Equity
The owner's equity is the amount of company assets that belongs to the owner of the company. It is calculated as the difference between the values of a person's assets and liabilities. The following formula best describes owner's equity:

Owner's Equity = Assets – Liabilities
Hence, if the value of your assets is greater than the value of your liabilities, then you have positive owner's equity. If the value of your assets is less than the value of your liabilities, then you have negative owner's equity. An equity and liabilities account looks something like this:

Equity & Liabilities	
Owner Mr. Alfin Deposit Capital Stock PT. Global 1 Dec 21	$500000

Debit and Credit
Debits and credits describe transactions. For every transaction, there is an equal and opposite Debit/Credit entry. It is important to remember that debits or credits are neither positive nor negative values. The entry under an account is a debit or a credit, not a positive or a negative value.

Asset and expense accounts increase in value when debited and decrease when credited. Liability, equity, and revenue accounts decrease in value when debited and increase when credited.
How do we know when to use credit or debit? We use the following table as a guideline:

	Increase	Decrease
Assets	Debit	Credit
Liabilities	Credit	Debit
Income	Credit	Debit
Expenses	Debit	Credit

Hence, with reference to the above table, when there is an increase in an asset item, we record that as a debit entry (value is placed under the debit column). Vice versa, a decrease in an asset item would be recorded under the credit column.

The following is a summary of transactions that occurred in the form of a general journal during the period December 2021 :

Date	Account Titles and Explanation	Ref	Debit	Credit
1 Dec 21	Cash		500.000	
	Capital Stock			500.000
2 Dec 21	Office Building		300.000	
	Cash			300.000
3 Dec 21	Office Furniture		800	
	Cash			800

5 Dec 21	Cash Sales Revenue from Product		2.000	 2.000
9 Dec 21	Cash Sales Revenue from Services Provided		1.000	 1.000
19 Dec 21	Purchase of New Machinery Cash		1.000	 1.000
20 Dec	Utility Bills for Dec 21 Cash		500	 500
26 Dec 21	Money Payable to Supplier Cash		2.000	 2.000
30 Dec 21	Monthly Wages Payable to Employees Cash		1.000	 1.000
	TOTAL		**808.300**	**808.300**

After the general journal, proceed to the summary of transactions trial balance during the December 2021 period as below :

PT. GLOBAL
Trial Balance
December 31, 2021

	Debit	**Credit**
Cash	197.700	
Office Building	300.000	
Office Furniture	800	
Purchase of New Machinery	1.000	
Sales Revenue from Product	2.000	
Sales Revenue from Services Provided	1.000	
Capital Stock		500.000
Money Payable to Supplier		2.000
Monthly Wages Payable to Employees		1.000
Utility Bills for Dec 21	500	
	503.000	**503.000**

4.2 DISCUSSION

Accounting activities, which are a long process from identification, measurement, to financial information must be correct and accurate. This is because the accounting financial statements can be the basis for every businessman or company for making business decisions. Even so, in the recording process, companies and business people themselves often make mistakes, which ultimately lead to losses and loss of trust from other parties.

As much as possible, errors in the accounting financial statements of your company or business, are made correctly without any fatal errors. Then what are the errors in the accounting process that often occur, here are the reviews:

1. Not careful enough to keep transaction evidence

   Not a few business owners who are less careful to keep transactions evidence or business expense receipts. In fact, these failures can lead to tax, accounting and cash flow problems for the company. Although it sounds trivial, transactions evidence is very important for your accounting activities.

   Remember that receipts and notes can be valid evidence when there are discrepancies in the numbers when examining your company's financial statements. Receipts and notes are also very useful and reliable to simplify the audit and taxation process.

2. Company Receivable

   In business, getting paid is certainly one of the most enjoyable things. However, you must be thorough enough to keep track of your business receivables. When you send an invoice, it means the receivables will be recorded and the customer owes you money. When the receivables is paid, the invoice status will change to paid. The process of calculating these receivables must be clear so that your business profits run smoothly.

   The problem is, the calculation of the company's receivables does not always run smoothly. Sometimes there can be errors in the recording of accounts receivable and you don't have enough time to correct them. You must solve accounting problems related to company receivables properly and accurately, so that can’t cause financial losses to your company or business.

3. Make the report only as a record

   For some business people, accounting may only be seen as the process of recording company financial data. Its function is nothing more than calculating company balances or tax interests. In fact, accounting has a bigger role.

   Financial statements are able to present a variety of information that can be taken into consideration in making decisions. Making decisions and determining business development strategies based on financial reports certainly increases the potential for your business development.

4. Counting error

   Accuracy is the most important thing in the accounting process. Moreover, accounting provides financial information for your company, so data inaccuracies will certainly harm you. Errors when calculating can not only happen to entrepreneurs, but also experienced accountants. Counting errors may occur when the accountant is in a hurry or is tired so that he is unable to detect the calculation errors that occur.

   You should not underestimate this calculation error. Because if the error when counting is combined with errors when inputting and reconciling, it will be a big error to the company's financial statements. If the error is not known for a long period of time, for example months, it will trigger a much more complex problem. More complex problems will certainly make the repair and resolution process more difficult to do.

5. Error writing decimal

This one accounting problem may occur if you are still using manual recording. For example, you want to write Rp. 1,000,000, but you write it wrong until it becomes Rp. 10,000,000. Of course this decimal writing error will greatly affect your financial statements. Therefore, you must be very careful about writing decimals, so that mistakes can’t repeat and can’t cause data errors in financial statements.

5. CONCLUSSION

The company's bookkeeping will help to find out whether the company is making a profit or is experiencing a loss. Therefore, bookkeeping is very important role in the continuity of a company.

However, there are times when in the bookkeeping process, you encounter problems that damage the company's financial statements. To be able to improve the company's books, here are the easy ways you can take :

Find out where the error

The location of errors in the company's books can be of various types. In some cases, errors can be found in the tax department, sometimes there are also discrepancies in data entry, or even related to inconsistent reconciliations. Find the error and know exactly how to solve the problem.

Don't forget to reconcile with the bank

The company will reconcile with the bank at the end of every month or even carry out this process only when they need it. So that the company's bookkeeping is not problematic in the future, it is better to carry out the reconciliation process with the bank as a daily routine to ensure the company's financial transactions. By carrying out the reconciliation process regularly and consistently, you can find out cash flow in detail and can also make time efficiency.

Consult with experts

At one point when making repairs to problematic bookkeeping, you may run into difficulties that you can't solve on your own. Therefore, so that the process of improving the company's bookkeeping can continue, it is possible to consult people who are considered more experts in the field of bookkeeping.

Take advantage of technology

Avoid a number of accounting problems that often occur as mentioned above to produce precise and accurate financial reports. To minimize errors that can cause accounting problems, you should start considering using Leukeun Accounting software which can detect recording errors so that accounting errors can be minimized by optimal. Besides that, with the accounting software, the management of data recording of all financial transactions is no longer complicated and systemized automatically without having to go through a complicated manual calculation process that is prone to errors.

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