Elements and Structure of Accounting Thought: A Conceptual Approach

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Abstract

This study seeks to discuss accounting theory's elements and structures using a conceptual approach, and it also emphasizes that accounting theory/thought is only useful when exemplified. The purpose of this work is to understand the divergent interpretations many scholars have given to accounting theory, its elements, structures and conceptual framework. In pursuance of the foregoing objective, relevant research data were generated using internet sources, journal articles and literature reviews. The study revealed that accounting theory's elements, structure and conceptual framework are the basic foundations of financial reporting practice. This paper therefore, enjoins accountants and other financial experts to always exemplify the accounting theory's elements, structure and conceptual framework they have painstakingly studied and understood. The knowledge derived from this work will assist financial experts and corporate managers in tackling the various financial frauds that have bedeviled the corporate world.

Keywords: Accounting Theory, Elements of Accounting, Structure of Accounting Theory and Concepts, Accounting thought

INTRODUCTION

Besides book-keeping which forms the bedrock of accountancy, accounting theory/thought plays a major role in financial reporting. This role is that of ensuring that the ultimate objective of financial reporting is achieved. Studying and understanding accounting theory and its elements and structures have therefore become inevitable (Coetsee, 2010). The preceding line of reasoning regarding the role of theory and thoughts in science has been well received in the discipline of accounting. There is still a growing need for the accounting profession to bring theory and practice into alignment. Studying and understanding accounting theory and its constituents have become inevitable due to high incidences of embezzlements, financial statements and payroll frauds, budget padding and all other forms of accounting frauds not mentioned here (Osho & Adebambo, 2018). Globally, trillions of naira are lost on daily basis by individuals, businesses and governments because basic principles which guide financial accounting and reporting are jettisoned. The gap between accounting theory and financial accounting and reporting practices are widening by the day. Precepts are useful only when they are exemplified.

Accounting theory and its elements and structures have been properly defined and explained in the existing literature to reflect both their interpretations, objectives and conceptual framework (Shohaimay, 2014). However, just studying and understanding accounting rules is not sufficient for the improvement of financial reporting practices. These researchers have not come across any study that specifically discussed the need to align the elements, structures and conceptual framework of accounting with accounting practices. Too much emphasis is presently being laid on just teaching accounting theory with less emphasis on exemplifying the theory and improving accounting practices. The current paper is therefore, an attempt to fill this gap. In this short paper, we are going to succinctly explain as follows: accounting theory, classification of accounting theory, elements of accounting theory, structures of accounting theory and the conceptual framework for financial accounting and reporting.

LITERATURE REVIEW

Conceptual Clarifications

Accounting Theory and Thought

Many people assume that, despite many attempts made to formulate one, a single widely accepted accounting theory does not exist. But Hendriksen (1977) describes accounting theory as a consistent collection of hypothetical, conceptual and pragmatic concepts that form the general reference structure for a field of study. Womlib.ru supports this concept, which asserts that accounting theory consists of broad, logically organized concepts. The two definitions use the words coherent and logically interchangeably, suggesting that accounting theory often discovers the orderliness that is normally present in a theory. Hendriksen (1977) and McDonald (1972) claim that it should be possible to establish an accounting theory using the three elements that McDonald claims must be present in each theory. According to him, these components are the encoding of phenomena into abstract representation (e.g. debit and credit), the manipulation and combination of laws (e.g. the presence of rules and regulations for the manipulation or combination of debits and credits) and the conversion back to real-world phenomena of debits and credits (e.g. presenting the debits and credits to users in the form of financial reports). This sounds like thought/ theory, obviously, and if so, it should specifically instruct us on how to plan and present information to users. This will also prevent numerous accounting procedures from being present. The most important goal of accounting theory is to provide a consistent collection of principles for the assessment and advancement of sound accounting practices that shape the general frame of reference. Therefore, accounting theory/ thought provides the basis for forecasting and describing the actions and events in accounting.

Elements of Accounting Theory

Accounting theory has three basic elements namely, (1) usefulness, (2) relevance, reliability, comparability and consistency and (3) four points all preparers of financial statements should know and recognized. A brief explanation of these elements is given below:

Usefulness

For a useful financial statement to be created, accounting should be effective. What this means is that only important and accurate information that informs the users about the financial condition of the entity should be included in the financial statements i.e. information that will enable the users to make accurate business and investment decisions.

Relevance, reliability, comparability and consistency

These are the qualitative characteristics of the information in the financial statement. Each of them as provided by Accounting Tools (2018) are considered briefly as follows:

Relevance

The information must be relevant to the needs of the users, which is the case when the information influences the economic decisions of users. This may involve reporting particularly relevant information, or information whose omission or misstatement could influence the economic decisions of users.

Reliability

The information must be free of material error and bias, and not misleading. Thus, the information should faithfully represent transactionsand other events, reflect the underlying substance of events, and prudently represent estimates and uncertainties through proper disclosure.

Comparability

The information must be comparable to the financial informationpresented for other accounting periods, so that users can identify trends in the performance and financial positionof the reporting entity.

Consistency

This suggests that imilar items should be given similar accounting treatments.
There are four basic assumptions that all financial professionals should operate under and these are also listed and explain below;

i. **Business Entity:** Every economic unit regardless of its legal form of existence is treated as a separate entity from parties having economic or proprietary interests in it. i.e. the business is separated from its owners.
ii. **Periodicity:** The business community and users of financial statements divide business results into accounting periods.
iii. **Going concern:** A business enterprise will continue in operational existence for the foreseeable future. The business does not intend to liquidate or curtail its activities.
iv. **Money as a Unit of Measure:** Naira and other relevant currency amounts are the only units of measurement used on financial statements.

Structure of Accounting Thought and Theory

Postulates, definitions and standards make up the structure of accounting theory. Without a general consensus as to what they precisely mean, these words are commonly used. Codification of accounting postulates and principles is the underlying reason for establishing the framework of accounting theory, according to Essa (n.d) and Course Hero.com (n.d), while the second underlying reason is to formulate a consistent accounting theory that will increase the consistency of financial reporting. According to Essa, postulates are self-evident statements that adhere to the purpose of financial statements. However, Hendriksen as cited in Essa (n.d) sees postulates as fundamental assumptions about the economic, political and sociological environment in which accounting must work. According to Essa (n.d), accounting concepts can be the root of those values and he further claimed that it is somewhat simplistic to think of the egg as a precedent for the chicken. Essa also sees concepts as being incompletely described as a mental pattern of similar ideas that, as more and more applicable instances become understood, evolve into an interconnected complex.

According to Essa (n.d) the accounting standards are general judgment rules derived from the accounting purpose and from the theoretical concepts of accounting. This author further argues that the development of accounting methods is often governed by these accounting goals and their theoretical principles. According to him, accounting methods are basic guidelines derived from accounting standards for accounting for particular transactions and events encountered by an accounting agency. According to Muiz (n.d), postulates are fundamental concepts that cannot be confirmed in formal logical structures, also called axioms, while principles are empirically checked rules that can become laws and general methods used to recognize and quantify accounting events. This author then argues that concepts are abstract concepts generalized from unique instances that are not part of the formal formulation of the theory. Persson (2016) argues that presumption is another term for postulate. According to him, both phrases refer to thoughts that we cannot understand as facts of business life, and yet are necessary as a basis for addressing accounting principles. This author further added that under accounting technology, they can be viewed as compact verbalizations of basic principles that function as foundation stones. As Munteanu and Berechet (2014) put it, postulates are basic principles, expected to be valid for the statement of certain arguments or for the study and creation of certain concepts. Postulates are often seen as axioms by the authors, which must not be defended. What some writers call postulates are referred to by other writers as definitions or principles, and vice versa, as the framework of accounting theory would further suggest.

Accounting Postulates

The basic Accounting postulate encompasses; Entity postulate, Going concern postulate, Unit of measure postulate and Accounting period postulate.

Accounting Concepts
Accounting Concepts on the other hand encompasses; Money measurement, Entity, Going concern, Cost, Dual aspect, Accounting period, Conservatism, Realization, Matching, Consistency and Materiality.

Accounting Principles

Consequently, Accounting principles encompasses; Cost principle, Revenue principle, Matching principle, Objectivity principle, Consistency principle, Full disclosure principle, Conservatism, Materiality principle, Uniformity and Comparability principle.

Fundamental Concepts Of Accounting

This is best understood by the comparision below;

Assumptions of Accounting:	Principles of Accounting:
1. Separate-entity assumption.	Cost Principles.
2. Continuity assumption.	Revenue Principle.
3. Unit-of-measure assumption.	Matching Principle.
4. Time-period assumption.	Full-disclosure Principle.

Thus, it can be observed that finding a precise terminology has always been one of the most difficult task in accounting. Further, the lack of agreement about their precise meanings has affected, to some extent, the attempts made towards developing a theory for financial accounting. Of essence is to explain things which are widely accepted as of greatest importance and widest applicability, whether as postulates, concepts or principles.

LITERATURE REVIEW

Conceptual Framework

Accounting Theory

Accounting theory is categorized into: Pragmatic approach which has to do with observing the conduct of accountants or those who use the information provided by them. Syntactic approach: logical argument, based on a set of premises. Semantic approach – concern with the way theories correspond to real-world events. Normative approach – based on semantic and syntactic. Positive approach – test hypotheses against actual events. Naturalistic approach – individual case studies and field work- do not try to generalize. The scientific approach – the world as an objective reality. Issues for auditing theory construction – use of normative and positive approaches when conducting auditing exercises. (Hendriksen, 1977 as cited in Womlib.ru, n.d.; Lenalena123, 2012; Tomkins and Groves, 2017)

Descriptive pragmatic approach

This is based on observed behavior of accountants and it is a theory developed from how accountants act in certain situations. The test is done by observing whether accountants do act in the way the theory suggests. This approach is an inductive one and it is criticized for the following reasons: does not consider the quality of an accountant's action, does not provide for accounting practices to be challenged and focuses on Accountants behavior not on measuring the attributes of the firm.

Psychological pragmatic approach

This depends on observations of the reactions of users to the accountants‟ outputs. This reaction is taken as evidence that the outputs are useful and contain relevant information. This approach is also criticized for the following reasons: some users may react in an illogical manner, some users might have a preconditioned response and some users may not react when they should. Theories are therefore tested using large samples of people. An example of an issue that might be resolved using this approach is the behaviour of investors to the release of accounting data.

Syntactic Approach

This approach represents the logical relations in the theory. It concerns the rules of the language employed, for example, the rules of grammar for English or accounting procedures or accounting equation. This theory becomes useful and realistic only when its contents correspond to real world situation. This is what is sometimes called rules of correspondence or operational definitions. One serious drawback here is that different types of monetary measures are added together.

Semantic Approach

Often this approach is referred to as correspondence laws or organizational concepts. It ties symbols, expressions, words or ideas with objects, events or functions in the real world, and this is what makes a theory seem plausible. The transactions and exchanges reported in vouchers, journals and ledgers are semantic inputs. Based on the premises and assumptions of historical cost accounting, the inputs are then manipulated. Semantics of output refer to measuring the output of the accounting system against any external reference, e.g. rises in earnings against changes in the share price. In motion, this is what one can call theory.

Normative Approach

If it is prescriptive in nature, a theory is normative. The 'golden era' of the 1950s and 1960s focused on policy recommendations, i.e. what should be. It focuses on the derivation of true income (profit) and practices based on analytical and empirical propositions that improve decision-usefulness. Financial statements should mean what they say. To some extent, the approach of IASB is a normative approach. An issue which can be resolved using this approach is „all accounting reports should be adjusted for inflation before they are released.

Positive Approach

This approach is an attempt to test hypotheses against actual events. It was expanded during the 1970s. It is based on experiences or facts of the real world. It explains the reasons for current practice and predicts the role of accounting information in decision-making. The main difference between normative and positive theories is that normative theories are prescriptive while positive theories are descriptive, explanatory or predictive. An example of one type of question that the positive approach will attempt to answer is 'what type of accounting do firms in one particular industry use for inventory before they release their accounting reports'?

Naturalistic Approach

The naturalistic approach begins from the view that truth and a result of human imagination are socially created. Truth, in other words, is not factual, but a product of the perceptions of circumstances and events encountered by individuals. This methodology is therefore best used to examine issues with a distinctive setting and no preconceived assumptions or hypotheses (such as the reaction of shareholders to the profit pronouncement of Champions' Breweries). It tries to solve individual problems, and so it may be difficult to generalize the outcome. Truth is perceived as a symbolic discourse, a social construction and as a projection of human imagination under this approach. In describing the response of an individual shareholder to investment-related announcements, the naturalistic approach is acceptable to use. This focuses on firm-specific issues. Using case study as a tool, this approach will try to address why the market is unimpressed with the success of Champion's Breweries, while during 2017-2018 it has generated improved profits.

Scientific Approach

This has an underlying premise that an objective truth is the universe to be investigated and it is carried out by gradual hypotheses. The implicit assumption here is that, under conditions that are constant through businesses, industries and time, a good theory holds. Scientific method opponents are of the belief that large-scale statistical analysis attempts to group something together. This is carried out in conditions that are frequently far from the world of accountants or their concerns. Truth is seen as a concrete framework, a concrete mechanism and as a contextual area of knowledge under a scientific approach. According to Schiell, Borba and Murcia (2010); Latour (1989) and Whitley (1984) as cited in Course Hero.com (n.d), the sociological and discursive perspectives of the empirical method, are essentially defined by the degree and strength of its contact with society. Input, process, and output accounting is seen as a socio-systemic structure. There is high interdependence between science and society. Misconceptions of intent make academics out of accounting professionals. Scholars are teachers. There is the need for 'absolute truth.' The scientific methodology does not state that 'truth' is given. This aims to provide convincing proof that can describe, explain, or foresee. It is reasonable to use this approach to explain 'the answer to the release of accounting data of all stock prices and why.'

Issues for Auditing Theory Construction

Auditing is a method of inspection applied to accounting inputs and procedures. Auditors give an opinion on whether the financial statements are compliant with the relevant reporting system as to whether the reports give a true and fair view. Focus on the conduct of an audit: identification of fraud, discovery of concepts of error and the essence of account verification. Mautz and Sharaf (1961) as cited in Almeida (2015) attempted to provide a detailed auditing theory in order to avoid the view that auditing was a realistic activity that did not involve theoretical growth. It consists of concepts such as proof, due audit care, equal representation, autonomy and ethical behavior. A normative approach to auditing theory coincided with the normative age of accounting. A constructive approach to auditing philosophy has contributed to the positive age of accounting.

Theoretical Framework

Agency theory

The relationship between accounting theory and financial reporting practice provide the mitigating measures which prevents the agent from pursuing self-interest when his principal entrust resources with him the agent.

Stewardship theory

A steward is motivated not by self-interest but by what he is mandated by his master to do and by what he is responsible for. This is made possible by compliance with laid down rules which also align accounting theory and practice.

Accountability theory

Evidence must be provided for the use of resources and the rules for doing so is also implicit in the accounting theory which also guide financial reporting practice.

METHODOLOGY

This is a qualitative study that basically relied on secondary sources of data. Data and information were collected from key and relevant journals and internet materials. This is to say this is an exploratory research.

RESULT AND DISCUSSION

In discussing the framework for Financial Accounting and Reporting, the 2018 revised Conceptual Framework comes to mind and it basically sets out the following;

i. The goal of financial statements for general purposes;
ii. The qualitative features of valuable financial information;
iii. The definition and boundaries of the reporting entity;
iv. Definitions of an asset, responsibility, equity, revenue and expenditure, and instructions to support these definitions;
v. Requirements for the inclusion in financial statements of assets and liabilities (recognition) and instructions on when to delete them (de-recognition);
vi. Bases of measurement and recommendations on when to use them;
vii. Concepts and guidelines on presentation and disclosure; and
viii. Capital and capital repair principles.

Useful Facts about the Accounting Conceptual Framework

Some of the fundamental general concepts of accounting have already been outlined. The incompatible and non-prescriptive nature of these concepts make it impossible to create a coherent conceptual framework. Since 1970, a number of moves have been made to create some form of more coherent conceptual framework. In 1989, the IASB version, known as the Framework for the Preparation and Presentation of Financial Statements, was issued. This version belongs to the category of conceptual frameworks developed in countries where private sector accounting standard setters exist. What guides the setting of standards is the assembling of interrelated concepts or a body of accounting theory. Conceptual framework may therefore, be considered as attempts to assemble interrelated concepts that will guide in the setting of standards. This assembling of related concepts will enable standards to be set on a consistent basis and not in an ad hoc manner. Attention should therefore, be paid to conceptual coherence and the development process should involve conceptual tidying-up.

Conceptual framework may be thought of as devices for conferring legitimacy and authority on a private sector standard setter that lacks legal authority of a public body. IASB which is a private sector accounting standard setter share these reasons too because they too need this legitimacy and authority or else it would not be able to achieve a broader international applicability. Conceptual framework development is based on the identification of good practice since principles are derived inductively from good practice. The criteria for identifying good practice are usually related to the assumed objectives of financial reporting. Any accounting practice that will not assist in achieving these objectives is therefore, not a good practice. Conceptual framework may be written in a prescriptive style or descriptive style or a mixture of both. Conceptual frameworks are normative since they are principles that guide the in setting and interpreting accounting standards. However, such guidance does not preclude a standard being issued that (for compelling pragmatic reasons) departs from a principle set out in the applicable conceptual framework.

Conceptual Framework for Financial Reporting

Based on what we have learnt so far, a conceptual framework consists of principles which are derived from conceptual coherence, conceptual tidying-up and good practice and used as guidance for setting and interpreting accounting standards that prescribe how financial statements should be prepared and presented. Consequently, the purpose of the framework is stated as follows**:**

1. To assist in the development of new standards and the review of current standards.
2. To assist in facilitating the harmonization of legislation, accounting principles and procedures concerning the reporting of financial statements.
3. To provide a basis for reducing the number of alternative treatments for accounting allowed by the standards
4. Assistance of national standards-setting bodies with the production of national standards
5. To support the preparers of financial statements in the application of IASs and in dealing with subjects which are not yet covered by the IAS;
6. To assist auditors in formulating an opinion on the compliance of the financial statements with the IASs;
7. Helping users of financial statements to view the details found in financial statements prepared in compliance with the IASs;
8. To provide information about its approach to the formulation of accounting principles to those who are interested in the work of the IASC.

The Framework is focused on „general purpose financial statements", including consolidated financial statements which are prepared and presented annually for the information need of various users. Special purpose reports like prospectuses and tax computations are not included in the framework. Financial statements of all commercial, industrial and business reporting enterprises, both in the private and public sectors are considered in the framework. The Framework first lists the users and their accounting information needs as follows:

Investors: should they buy, hold or sell their shares? Can the company pay dividends?
Employees: Can our enterprise provide remuneration, retirement benefits and employment opportunities?

Lenders: Will our loans and interest be paid when due?
Suppliers and other trade creditors: Will our money be paid in a short term? As major customers, should we depend on continuation of the business?
Customers: Will the business continue in the long term?
Governments and their agencies: Are their activities legitimate? Are they paying their taxes?
Public: Are these enterprises fulfilling their corporate social responsibilities? Are they patronizing our local suppliers?

Thus, the financial statements cannot satisfy or meet the information needs of all users but, there are needs which are common to all users.

Summary overall Objectives f Financial Statements as Contained in the Conceptual Framework

1. To illustrate the financial situation, the outcomes and the improvements in the financial position.
2. The goals set out above will allow users' popular needs to be met. These priorities restrict the provision of financial statements to only financial details. It is not provided with non-financial information.
3. With these goals in mind, users may assess the ability of an organization to generate cash and cash equivalents. The ability to pay staff, vendors, lenders and dividends, for example.
4. The financial condition is shown on the balance sheet. The income statement reveals the financial results and improvements in the financial condition are indicated by a different statement called the statement of changes in the financial position.
5. Different elements of the same transactions or other activities represent the component parts of the financial statements. Consequently, these components interlink. Even though each offers
Different information and none of them can fulfill all the information needs of users, none of the statements are likely to serve a single purpose.

In the design context, the different 'assumptions and characteristics' of accounting statements already considered under frameworks and elements of accounting theory are also included.

From the foregoing therefore, the following findings subsists with respect to the issue in question
1. Accounting theory facilitates the preparation of credible financial statements.
2. Elements of accounting theory set the rules for generating credible financial statements.
3. The structure of accounting theory consists of postulates, concepts and principles which are oftentimes used interchangeably.
4. The conceptual framework for financial accounting and reporting are derived from accounting theory's elements and structure.
5. The conceptual framework covers financial statement issues such as objectives of financial statement, qualitative characteristics of financial statement, elements of financial statements and capital.
6. Accounting theory lays the foundation for financial reporting practice.

Similarly, the knowledge which this study has added to the existing literature is that accounting theory's elements, structures and conceptual framework are useful to the extent that they are applied correctly and objectively. This knowledge is necessary especially in a world where financial statement frauds and other types of fraud occur on a frequent basis. Without appropriately exemplifying accounting theory and concepts, our financial accounting and reporting practices will continue to deteriorate.

CONCLUSION AND RECOMMENDATIONS

The accountant is able to prepare and present accurate financial statements through the analysis and understanding of accounting theory. Hendriksen and McDonald still maintain that it exists despite the argument made by many people that there is no single accounting theory, and they describe it as a consistent collection of broad principles that form a general structure for the assessment and development of sound accounting practices. Accounting theory is categorized by the writers and other researchers into seven approaches: pragmatic, syntactic, semantic, normative, constructive, naturalistic and scientific.The elements of accounting theory which highlight the rules for generating credible financial statements are classified into (1) usefulness, (2) relevance, reliability, comparability and consistency and (3) business entity, periodicity, going concern and money as a unit of measure. The structure of accounting theory with their controversial meanings and categorization consists of postulates, concepts and principles. Even though lack of agreement about their precise meanings has precluded the development of a theory for financial accounting, postulates, concepts and principles are still widely accepted and applied as rules that underlie the preparation and presentation of financial statements.

The conceptual framework which is derived from the elements and structures of accounting theory, consists of principles used in setting and interpreting accounting standards. The conceptual frameworks which are basically provided by IASB and IFRS Board are used to achieve the following objectives: develop and review standards, promote harmonization, reduce number of alternative accounting treatments, assist national standard setting bodies, assist preparers of financial statements, assist auditors in forming an opinion, assist users of financial statements and provide information to those who are interested in the work of IASC. The scope of the framework covers the following financial statement issues: objectives, qualitative characteristics, elements and capital. The Framework focuses on annual general purpose and consolidated financial statements of corporate institutions in the public and private sectors. It also lists the users of financial statements as investors, employees, lenders, suppliers, customers, government and their agencies and the public. The bases for preparing the conceptual framework are: conceptual coherence, conceptual tidying-up and good practice. Accountants, professional accountants, accounting instructors, financial regulators and other financial experts should rise to the challenge by teaching the principles of accounting theory, exemplifying the theory and improving accounting practice.

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