**Make It Meaningful**

**Financial information** is any record or data related to an individual’s or business’s financial activities. Think about your personal financial information. It might include records of:

* Credit card transactions
* Bank deposits and withdrawals
* Loans (school, car, house, etc.)
* Wages/Salary
* Bills (rent, utilities, wireless, etc.)
* Investments, savings accounts, and other **assets**

Can you think of more examples of personal financial information? (There are several free online resources for keeping track of your personal financial information. Check out [www.mint.com](http://www.mint.com) and more!)

Businesses must keep track of quite a bit of financial information as well. Here are just a few examples of financial data that a typical business generates:

* **Accounts payable** records

Accounts payable are debts a business owes (e.g., a bill for having new carpet installed). Accounts receivable represent money that is owed *to* a business (e.g., an outstanding sales invoice for a customer who bought raw materials from the company).

* **Accounts receivable** records
* Receipts
* Sales invoices
* Corporate credit card transactions
* Loan documents
* Expense reports
* Income statements
* Records of other assets

Can you think of more examples of a business’s financial information?

**Make it work**

Imagine a big desk piled high with papers—receipts, bank statements, pay stubs, bills, etc. That’s a lot of financial information! However, in its current state, it isn’t very useful. The data need to be gathered and organized in a way that makes sense. This is where the accounting function comes in. **Accounting** is the process of gathering, recording, organizing, and reporting financial data. Accounting makes a business’s financial information useful for any number of purposes (which we’ll learn more about in Objective B). A business’s accountants will, for example, use financial data to create a **balance sheet** (a snapshot of the business’s assets and **liabilities**) and an **income statement** (a record of the business’s financial performance over a certain period of time). These **financial statements** are very beneficial to a number of different internal and external users seeking more information about the company. (To learn more about financial statements, check out the short video and lesson at <http://education-portal.com/academy/lesson/what-are-the-financial-statements-definition-purpose-importance.html#lesson>.)

**Data and Information**

Don’t let the terms “data” and “information” confuse you. Data are raw facts and figures (that’s right—“data” is a plural word, even though it doesn’t sound like it!). Information is knowledge or facts presented in a usable form. However, many people tend to use the two terms interchangeably.

**Make it useful**

What makes financial information useful? The following four criteria are common standards for achieving this goal:

 ***Useful financial information is understandable*.** Have you ever purchased a product that required assembly—and then realized that the instructions were printed in a foreign language? Unless you had some very detailed photos to go by, the instructions probably weren’t of much use to you. That’s because they weren’t understandable!

 Financial information must be understandable, not just to the people who prepare it, but to everyone who needs to use it. Accountants and others in the field of finance may have in-depth knowledge of financial data, but their reports will be seen by managers, employees, investors, etc., who may not be as skilled in the finer points of financial interpretation. For this reason, useful financial information is presented in ways that are understandable, both in the language used and in the layout and format of the report.

 ***Useful financial information is relevant*.** A good definition of **relevant** is “appropriate to the situation at hand.” Let’s say you’re trying to determine whether or not you can afford to buy an iPad. While you’re checking your bank account’s balance, your sister mentions to you that she still has birthday money left and is thinking about purchasing an iPad herself. You’re happy for your sibling, but her financial information doesn’t help you with your decision. It’s *irrelevant*.

 With so many financial data available within a business, it can be difficult to distinguish what’s relevant from what’s irrelevant. The people who receive financial information need it to be applicable to their purposes. For example, a manager deciding whether or not to hire new employees may need to analyze a different set of financial data than a potential investor determining whether or not the company will provide a good **rate of return** for her/his money. Accountants must prepare their various reports with this in mind.

 In addition to being applicable to its audience, relevant financial information is also *timely*.
This means that it’s up to date. In many situations, outdated financial information is useless. Fortunately, advances in information technology have made keeping financial information current a much easier task for accountants. (For a bit more insight into the importance of timely financial statements, read this blurb from a financial consulting firm—<http://cfowise.com/solutions/improve-profit/accurate-timely-financial-statements>.)

 ***Useful financial information is reliable*.** When a user receives financial information, s/he should be able to safely assume that the information is accurate. This means that the information is not only error free but is also *complete*. Let’s say your friend sends you a text inviting you to a concert. He tells you where the concert is, what time it starts, and where he’ll meet you. This is all accurate information; however, since he hasn’t told you what *day* the concert is, the information is incomplete. It isn’t usable until you get all the data you need. The same goes for a business’s financial statements and reports.

 Another characteristic of reliable financial information is **neutrality**. Neutral means impartial or unbiased. When accountants prepare financial reports, they should focus on the numbers, not how they’ll be interpreted or analyzed by those who receive them. It might be tempting to present financial data in a way that makes the company look better (or worse, depending on the circumstances), but biased information is not reliable or useful. In addition, it’s unethical for accountants to attempt to influence users of financial information. They must stick to the facts!

 Reliable financial information also conforms to specific, common accounting standards. It wouldn’t be good if businesses made up their own rules and procedures for processing financial information! Think of it in these terms: What if every teacher in your school used a different grading scale? An “A” in one class might be a “B” in another. This would make your transcripts very difficult to interpret! That’s why a set of standards is necessary.

For a long time, U.S. businesses have used a system called **GAAP (Generally Accepted Accounting Principles)** as their guide for accounting practices and procedures. However, a newer system known as **IFRS (International Financial Reporting Standards)** is also gaining popularity and usage. You can learn more about the differences between the two systems here—<http://www.investopedia.com/ask/answers/09/ifrs-gaap.asp>. No matter what set of accounting standards a business chooses to use, it’s important to remain consistent and to let users know what system has been selected.

 ***Useful financial information is comparable*.** Users must be able to compare current financial information to past financial information. If they can’t, it’s impossible to see what financial changes have occurred in the business, either positive or negative. The same principle applies to your own life in many ways. For example, if you don’t have access to your basketball stats from last season, how can you know if you’ve done any better this year? Or, what if last season’s stats were recorded using a completely different method or format? That would also make the comparison quite difficult.

 A business’s financial information should also be comparable to data from similar businesses. Potential investors want to see how one company stacks up against another company in the same industry. Managers also want to know how their business is performing in relation to its competitors. Comparability is another reason businesses conform to widely accepted accounting standards—it provides across-the-board **consistency** that benefits everyone. Comparability and consistency go hand in hand; therefore, a business should choose a set of accounting standards to follow and change it only when absolutely necessary. (For more on the relationship between comparability and consistency, go to <http://accounting-simplified.com/financial-accounting/accounting-concepts-and-principles/comparability.html>.)

**Treat it right**

Even within the same set of accounting standards, there may be more than one acceptable way to “treat” (record and organize) a piece of financial information. Let’s work through a couple of examples.

 *You make a $15 payment to a web site that offers mp3 downloads for 10 cents each. The company receives your money in one lump sum, but it will provide its service to you over a period of time (however long it takes you to download 150 songs). The expenses involved in providing the service to you cost the company around $3. So, that’s $15 coming in and $3 going out. However, the $3 doesn’t go out at the exact same time the $15 comes in. The company can spend your money immediately if it wants to, but its accountants must determine how they will keep track of the expenses involved in providing the service to you so that they don’t become lost or hidden. There may be more than one acceptable accounting method for tracking these expenses, but the important thing is to do it the same way* every time.

*You have a summer job babysitting your neighbors’ two children. At the beginning of each week, your neighbor gives you $100 in cash for the kids’ weekly expenses (pool, ice cream, etc.). It is your job to keep track of what you do with that $100. You might keep a little notebook where you jot down each expense. Or, you might put $20 in five different envelopes marked for each day of the week. However you treat the financial information, you should be consistent and careful so you don’t lose track.*

 Make sense? Can you think of different ways you might “treat” a piece of your personal financial information?

**Summary**

Financial informationis any record or data related to an individual’s or business’s financial activities. Accounting is the process of gathering, recording, organizing, and reporting financial information to those who need it. The accounting process should make financial data useful—understandable, relevant, reliable, and comparable. Every business must choose a set of accounting standards to conform to. Consistency is key—even when there is more than one acceptable way to “treat” a piece of financial information, the business must use the same method each time.