BUSS1030
SUMMARY NOTES
SEMESTER 2, 2018

INTRODUCTION TO ACCOUNTING

WHAT IS ACCOUNTING?

- Accounting is concerned with the **collection**, **analysis** and **communication** of economic information (CAC)
- Aim of accounting: The **most accurate** representation of the economic state of an entity
- Such information can be used as a tool of **decision making, planning** and **control** (D, M, P, C)

Business Operations
- Need to balance between risk and return
    - **Return:** The gain that results from a particular event or occurrence.
    - **Risk:** The likelihood that what is projected to occur will not actually occur.
- Wealth enhancement as the main objective of a business
- Accounting is central to all businesses

What is the primary objective of financial reporting?
- To provide information useful for making investment and lending decisions
    - For the needs of various **stakeholders**
    - Owners, customers, competitors, government, suppliers, managers, community representatives, lenders

Financial Accounting	Management Accounting
External users make decisions about the entity. E.g. Investors - Financial accounting is the preparation and presentation of financial information to allow users to make economic decisions about the entity - Includes: The income statement, the balance sheet, the cash flow statement – **Financial Statement Analysis** - More legal restrictions - Mainly historical/broad overview/predictable periods	Internal users make decisions about the entity. E.g. Management - Core activities include formulating **plans and budgets** - Information used in monitoring and control within the entity - Both past and future/Quite detailed/Whenever required

Seven Fundamental Qualities
- Relevance, faithful representation (key characteristics); comparability, verifiability, timeliness, understandability, cost-benefit (enhancing characteristics)

4-Step Process: Information… Identification, Recording, Analysis, Reporting (IRAR)

OVERVIEW OF MAIN FINANCIAL REPORTS

3 Main Reports used in Financial Accounting:
1. Statement of Cash Flows
    - What cash movements took place over a particular period

KEY ACCOUNTING CONCEPTS

Account: Account names describe an account and record the impact of events effecting value of Assets, Liabilities or OE
Transaction: Event that involves at least two parties exchanging resources
Note: Agreeing, discussing, thinking about ≠ business transaction

FINANCIAL STATEMENTS

Statement of Financial Position (Balance Sheet)	Reports the Assets, Liabilities and OE of the business at a point in time
Statement of Comprehensive Income	Summary of an entity's income, expenses and changes in equity (E.g. New owner investments and drawings)
Income Statement	Reports revenues and expenses to measure a profit or loss
Statement of Cash Flows	The statement that shows the sources and uses of cash for a period, classified according to the entity's major activities (operating, investing and financing)
Statement of Changes in Equity	Shows changes in OE as a result of transactions and events during a period
Receivable	Amounts owed to a business, regarded as assets
Profit	A financial gain
Equity	Net assets, the 'leftover' – less assets, less total liabilities

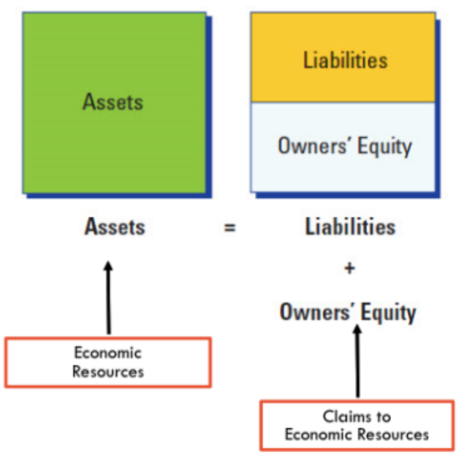
Journal: Chronological record of all recorded transactions
↓
Ledger: Shows the running balance of a specific account (Can be shown as a T-Account)
↓
Trial Balance: List of all ledger accounts along with their running balances

Chart of Accounts: Lists all the accounts a business uses along with account numbers

ACCOUNTING EQUATION

Measures the resources of a business and the claims to those resources.
Double-entry accounting:
- Means that we record the dual effects of each business transaction
- Must balance

<u>Claims against the asset of an entity:</u>
- External claims = Liability (Debt Holders Claim)
- Internal claims = Owner's Equity (Shareholders Claim)



OWNER'S EQUITY

Residual interest in the assets of the entity after deducting all of its liabilities. Purpose of a business is ↑OE.

Comprised of many parts:

Capital	Drawings	Revenues	Expenses
Owner invests assets in business. Credit Acc.	Owner withdrawals for personal use. Debit Acc.	Amounts received or to be received from customers for sales of products or services Credit Acc.	Amounts that have been paid or will be paid later for costs that have been incurred to earn revenue. Debit Acc.

<u>REMEMBER</u>

- **Revenues are recorded when earned, and expenses are recorded when incurred –** because of Accrual Accounting
- Profit or loss = Revenue – Expenses **(retained profit)**
    - Ie. Revenue increases equity (inflow), while expenses decrease your equity
- When you use an asset, you end up with an expense

TYPICAL ACCOUNT NAMES

	Account Number		Account Title
Assets	101		Cash at bank
	102		Accounts receivable
	103		Supplies
	104		Prepaid Insurance
	105		Delivery vehicles
	106		Accumulated depreciation – Delivery vehicles
	107		Computer equipment
	108		Accumulated depreciation – Computer equipment
Liabilities	201		Accounts payable
	202		Bank loan
OE	301	- capital	Share capital
	401	revenue	Delivery revenue – cash
	402		Delivery revenue – credit
	403		Interest revenue
	501	expenses	Salaries expense
	506		Insurance expense
	507		Telecommunications expense
	508		Rent expense
	509		Advertising expense
	510		Electricity expense
	511		Depreciation expense – Delivery vehicles
	512		Depreciation expense – Computer equipment
	513		Bank charges
	514		Leasing expense
	515		Supplies expense

PLANNING AND BUDGETS

Purpose of Planning and Control

- To fulfil corporate objectives:
  - Goals of business (E.g. Wealth enhancement)
  - Mission statement (Broad intent)
  - Position statement (Where the business is currently placed relative to where it wants to be)
  - Vision statement
- **Control:** Defined as compelling events to conform to plan – accounting information should highlight variances between budget and actual outcomes

Types of Plans and Budgets

Long-Term (Strategic) Plan

- Defines the general direction of the business over the next five or so years
- Although, depends on industry and rate of change (5 years in IT business would be too long)

Budget

- Short-term financial plan, usually 12 months

Note: Budgets are heavily interrelated and linked. Sales budget is most important part and used as a starting point/'master' budget – if your sales forecast is wrong, your budget will not be very helpful.

Budget Committee	**Group of managers formed to supervise the budget-setting process**
Budget Officer	Individual (often an accountant) appointed as responsible for the tasks of the budget committee
Top-down	Senior management of each budget area originates the budget targets
Bottom-up	Great weight given to views of relatively junior stuff when budget setting (more effective, but more time consuming)
Incremental budgeting	Approach which uses what happened last year as a starting point for this year's budget (referred to as discretionary budgets)
Zero-based budgeting	A budget process which starts with the assumption that everything must be justified/no reliance on previous periods

Note: Most organisations use a combination of top-down and bottom-up

Benefits of Budgeting

- Promotes forward-thinking
- Motivates managers
- Basis for a system of control
- Helps coordinate various sections of the business
- Provides a system of authorisation

PROJECTED/FORECAST STATEMENTS

- Valuable for developing long-term strategic plans
- Identify future financial needs
- Most commonly prepared on the basis of an **optimistic** view of likely future events

STATEMENTS SUMMARY

General Journal

General Journal (GJ1)

Date	Description	Account Number	Debit	Credit
Sep 1	Cash at bank	101	42,000	
	Capital			42,000
	(Owner contributed capital)			

(Tick right hand side once moved to general ledger)

General Ledger

General Ledger

Cash at Bank 101

Date	Explanation	Post Ref	Debit	Credit	Balance	
	Opening balance				0	
Sep 1	Capital	GJ1	42,000		42,000	Dr
Sep 6	Service Revenue	GJ1	1,400		43,400	Dr

T-Account

T-ACCOUNT

Cash at Bank	101
Jan 1 Capital GJ1 100,000	Jan 1 Inventory GJ1 40,000
Jan 1 Bank Loan GJ1 100,000	Jan 4 Machine GJ1 10,000
	Jan 5 Prepaid Rent GJ1 5,000
	Jan 7 Wages Expense GJ2 1,000
	Jan 8 Accounts Payable GJ2 5,000
	Jan 9 Drawings GJ2 2,000
	Jan 31 Closing Balance 137,000
200,000	200,000
Feb 1 Opening Balance 137,000	

Trial Balance

Paula Lee eTravel
Trial Balance
30 June 20X0

	Balance	
Account Title	**Debit**	
Cash at bank	$19 900	
Accounts receivable	2 000	
Office supplies	500	
Land	11 000	
Accounts payable		$200
Paula Lee, capital		30 000
Paula Lee, drawings	2 000	
Service revenue		8 500
Rent expense, computer	600	
Rent expense, office	1 100	
Salary expense	1 200	
Electricity and gas expense	400	
Total	$38 700	$38 700