THE ACCOUNTING ENVIRONMENT

ACCOUNTING AND IT'S ROLE IN SOCIETY

Accounting is an information system that identifies, records and communicates* the economic events of an organisation to interested users.
*The 'accounting process'.

Accounting involves the entire process of economic events whereas bookkeeping involves only the recording element.

The roles of accounting are to; provide a means of communicating and measuring business activity and the financial information required for making decisions in regard to money and business.

Internal Users – individuals who plan, organise and run the company.
External Users – investors, creditors and government.

SOURCES OF ACCOUNTING REGULATION

Accounting regulation aims to protect the users of accounting data.

Conceptual framework sets out the concepts that underlie the preparation and presentation of financial statements for external users.

AASB – Australian Accounting Standards Board
GAAP – Generally Accepted Accounting Procedures

Corporate Social Responsibility (CSR) is concerned with issues relating to a company's social, environmental and governance.

Integrated Reporting consists of concise communication, about how an organisations strategy, governance, performance and prospects in terms of its external environment can lead to the creation of value. It is required globally to promotes financial stability and sustainable development.

Global Reporting Initiative (GRI) refers to how an entity must report against; direct economic impact, environmental impacts, labour practices and decent work, society and product responsibility.

CONCEPT OF BUSINESS AND 'ENTITY'

A business is an enterprise that provides products or services desired by customers.

Accounting Assumptions

Monetary unit – Only data that can be expressed in terms of money is included in the accounting records.

Economic entity – Activities of an entity must be 'kept separate' from activities of the owner and all other economic entities.

Public	Business is owned and operated by government or local authorities.
Private	Business owned and operated by the individual.

Business Structures

Sole Proprietor
- Owned and operated by one person
- Contributes 'capital' and withdraws 'drawings'
- Entitled to all profits which are taxed as personal income

- Unlimited liability

Partnerships

- A business jointly owned and operated by two or more legal persons
- Unlimited liability

Company

- A legal entity that is separate to the owners
- Controlled by directors and regulated by ASIC
- Limited liability
- Company corporate tax
- Distribution in dividends

*ASIC = Australian Securities & Investment Commission

Business based on activity:

1. Manufacturing involves the conversion of raw materials into finished goods.
2. Trading involves the buying of inventory and selling it.
3. Service provides a service to a customer.

THE CLASSIFICATION AND ANALYSIS OF BUSINESS TRANSACTIONS

BUSINESS ENTITIES

Entity Assumption

Activities of the entity must be kept separate and distinct from activities of the owner and all other economic entities.

Trusts are legal relationships where a person holds and operates property for the benefit of someone else. The person makes trust distributions to beneficiaries.
*Reporting Entity Concept must produce 'General Purpose Financial Statements' (GPFS), which is regulated by GAAP.

BUSINESS TRANSACTIONS

A business transaction is an economic event of a business and has financial impact on the entity.

Classified > Analysed > Summarised

Cash accounting is when all business transactions are recorded when cash is actually received or paid.

Accrual accounting records revenues and expenses even if related cash has not changed hands.
*Accrual is the better option.

TRANSACTION ANALYSIS

Elements of accounting

Assets

Resources controlled by the entity that provides future economic benefit.

Liabilities

Debts and obligations of the entity that will result in future economic sacrifice.

Owners' Equity
The owners claim on the assets of the entity.

Revenue
Amount earned from the sales of goods or services.

Expenses
Costs incurred in running a business in order to earn income.

*Depreciation is the calculation of the value of non-assets which have been 'used up'.

Concept of duality refers to how every business transaction has a dual effect. E.g. Cash is drawn from the bank account to pay wages.

ASSETS = LIABILITIES + OWNERS EQUITY

OR

ASSETS = LIABILITIES + OWNERS EQUITY + (REVENUE – EXPENSES)

EXAMPLE:

	ASSETS	LIABILITIES	OWNERS EQUITY
1	+1500 Cash		+1500 Capital
2	+7000 Equipment -7000 Cash		
3	+1600 Supplies	+1600 Accounts Payable	
4	+1200 Cash		+1200 Service Revenue
5		+250 Accounts Payable	-250 Advertising Expense
6	+1500 Cash +2000 Accounts Receivable		+3500 Service Revenue
7	-1700 Cash		-600 Rent -900 Salaries -200 Utilities
8	-250 Cash	-250 Accounts Payable	
9	+600 Cash -600 Accounts Receivable		
10	-1300 Cash		-1300 Drawings

BUSINESS TRANSACTIONS IN JOURNALS AND LEDGERS

THE ACCOUNTING RECORDING PROCESS

1. Events
   The business will experience economic events that will result in a form of source document.

2. Journals
   Analyse the transaction and record in general journal.

3. Ledgers
   Each journal entry is then transferred to the relevant ledgers.

4. Trial Balance
   Periodically, the balance of each ledger is then transferred to the trial balance. An important error checking mechanism.

5. Reports
   Trial balance is split up and presented as income statement and balance sheets. Used by decision makers.

TRANSACTIONS IN THE GENERAL JOURNAL

General Journal Format

Date	Accounts	Debit (DR)	Credit (CR

Debit
- Increase an asset account
- Decrease a liability account
- Decrease an owners' equity account

Credit
- Decrease an asset
- Increase a liability
- Increase owners' equity account

Steps in journalising transactions
1. Which elements are affected?
2. Which specific accounts are affected?
3. Are the items increasing or decreasing?
4. For each account do we debit or credit?

Element	**Increase**	**Decrease**
Asset	DR	CR
Liability	CR	DR
Owner's Equity	CR	DR
Revenue	CR	DR
Expenses	DR	CR

*Total debit must always equal total credit