Accounting for business decisions A

Week 1

- ### Four Assumptions of accounting

1. **Economic entity**: financial activities of a business can be separated from the financial activities of the business's owner. This means that information for personal affairs of the owner is removed.
2. **Time Period assumption**: economic information can be captured and communicated over a short period of time.
3. **Monetary Unit assumption**: The dollar is the most effective means to communicate economic activity. If an economic activity cannot be expressed in dollars then it is not recorded in the accounting system
4. **Going concern assumption**: A company will continue to operate in the foreseeable future.

- ### The Statement of comprehensive income (Income statement)

- Report's a company's **revenues** (money gains results from the sale of goods or services) and **expenses** (decrease in resources resulting from the sale of goods or services)
- Its purpose is to demonstrate the financial success or failure of the company over that specific period of time.
- **Cost principle:** The principle that assets should be recorded and reported at the cost paid to acquire them.
- **Revenue – expenses= net profit or loss**
- **Multistep format:** have subtotal groups such as gross profit, profits before and after tax, while single step calculates total revenue and total expenses and them determines net profit in one step.
- **Vertical analysis:** account balance/net sales or revenue

Lawn Service
Statement of Comprehensive Income
For the month ending 31 January 2015

Revenues		$1120
Expenses:		
Fuel	$80	
Interest	5	
Depreciation	70	
Total expenses		155
Net profit (total comprehensive income)		$965

- ### Statement of Financial position (balance sheet)

- **Assets**: a resource of a business that will provide economic benefit. E.g. cash or land
- **Liabilities**: an obligation of a business that will require the sacrifice of economic resources at some future date. E.g. accounts payable

- **Equity**: the difference between a company's assets and liabilities and represents the share of assets that are claimed by the business's owner
- **Contributed capital:** The resources that investors contribute to a business in exchange for ownership interest.
- The statement of financial positions is the statement that shows a company's assets, liabilities and equity.

Lawn Service
Statement of financial position
At 31 January 2015

Cash	$194	Note payable (to Mum)	$200
Accounts receivable	120	Total liabilities	200
Supplies (petrol)	10	Contributed capital	100
Lawnmower	195	Retained earnings	234
Petrol can	15	Total equity	334
Total assets	$534	Total liab and equity	$534

- Assets = Liabilities = Owners Equity.
- Current assets are listed in order of their liquidity.
- Horizontal analysis: analysing financial statements over time to analyse changes in accounts occurring between years. Dollar and percentage changes are calculated on each item within financial statement.
- Vertical analysis: comparing account balances within one year. The analysis is calculated by dividing each account balance by a base account, yielding a percentage. **Accounting balance/total assets**
- Common size financial statements are statements in which all items have been restarted as percentage of a selected item on statements which is useful for comparing businesses of different sizes.

The Statement of changes in equity

- Shows the change in a company's equity and the changes in retained earnings over a specific period of time.
- **Retained earnings + net profit/loss – dividends= retained profits (ending balance)**
- Shows why each equity account has changed.
- Links income statement to balance sheet through retained earnings column,

Lawn Service
Statement of Retained Earnings
For the month ending 31 January 2015

Retained earnings, 1 June	$ 0
+ Net income (or Net profits)	965
– Drawings (Dividends)	731
Retained earnings, 30 June	234

The Cash flow Statement

- reports a business's sources and use of cash over a specific periods of time
- **Financing activities:** generating and repaying cash from creditors and investors. (money borrowed for the business) Raising funds.

Cash Flow Statement
For the month ending 31 January 2015

Operating activities	
Cash received from customers	$1000
Cash paid for petrol	(90)
Cash paid for interest	(5)
Net cash provided by operating activities	$905
Investing activities	
Cash paid for lawnmower	$(260)
Cash paid for petrol can	(20)
Net cash used by investing activities	(280)
Financing activities	
Cash received from borrowing	$ 200
Cash received from owner	100
Drawings (dividend)	(731)
Net cash used by financing activities	(431)
Net increase in cash	$194
Cash balance, 1 June	0
Cash balance, 30 June	$194

- **Investing activities:** the revenue generating assets that it acquired for operations. Long term to generate more profit.
- **Operating activities:** the purchase of supplies, the payment of employees and the sales of products. (things needed to operate the business) Every day regular activities.
- **Operating activities +/- investing activities+/- financing activities = Net increase (decrease) in cash.**