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**Executive Summary**

In this module, I able to brief about accounting fundamentals and three basic activities of accounting the economic events of a company. Additionally, I also annotate about double entry system and golden rule of accounting. Furthermore, I also study and focus about the classification of accounts. As well as that, on third part of this assignment, I describe about the balance sheet on the other hand, I also describe about cash flow statement. Finally, I illuminated in details on book-keeping and accounting in contrast, I able to explain in details about the branches of accounting.

**Introduction**

Accounting is a glorious but misunderstood field. The popular view is that it’s mostly mind-numbing number-crunching; it certainly has some of that, but it’s also rich intellectual pursuit with an abundance of compelling and controversial issues. Accountants are often stereotyped as soulless drones laboring listlessly in the bowels of corporate bureaucracies. But many accountants will tell you that it’s people skills, not technical knowledge, that are crucial to their success. And although it’s often thought of as a discipline of pinpoint exactitude with rigid rules, in practice accountants rely heavily on best estimates and educated guesses that require careful judgment and strong imagination.

Actually, stereotyping accounting and accountants,either positively or negatively, is useless because accounting involves so many different activities. The short-but-sweet description of accounting is “the language of business”. A more formal definition is offered by The American Accounting Association: “ The process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users of information.”

However defined, accounting plays a vital role in facilitating all forms of economic activity in the private, public and nonprofit sectors, in endeavors ranging from coal mining to community theater to municipal finance.

**QUESTION 1: In a brief but comprehensive response, define the role of accounting. ( 20 Marks )**

The name that looms largest in early accounting history is ***Luca Pacioli***, who is 1494 first described the system of double-entry bookkeeping used by Venetian merchants in his Summa de Arithmetica, Geometria, Proportioni et Proportionalita. Of course, businesses and governments had been recording business information long before the Venetians. But it was **Pacioli** who was the first to describe the system of debits and credits in journals and ledgers that is still the basic of today’s accounting systems.

The industrial revolution spurred the need for more advanced cost accounting systems, and the development or corporation created much classes of external capital providers - share owners and bondholders - who were not part of the firm’s management but had a vital interest in its result. The rising public status of accountants helped to transform accounting into a profession, first in the united kingdom and then in the united states. In 1887, thirst-one accountants joined together to create the American Association of public accountants. The first standardized test for accountants was given a decade later,and the first CPAs were licensed in 1896.

The Great Depression led to the creation of the Securities and Exchange Commission (SEC) in 1934. Henceforth all publicly-traded companies had to file periodic reports with the commission to be certified by members of the accounting profession. The American Institute of Certified Public Accountants (AICPA) and its predecessors had responsibility for setting accounting standards until 1973, when the Financial Accounting Standard Board (FASB) was established. The industrial thrived in the late 20th century, as the large accounting firms expanded their services beyond the traditional auditing function to many forms of consulting.

The Enron scandals in 2001, however, had broad repercussion for the accounting industry. One of the top firms, Arthur Andersen, went out of business and, under the Sarbanes-Oxley Act, accountants faced tougher restriction on their consulting engagement. One of the paradoxes of the professions, however, is that accounting scandals generate more work foe accountants, and demand for their services continued to boom throughout the early part of the 21st century.

**The Role of Accounting in Business**

Running a small business often requires owner to have experience in various business functions. Producing goods or service, conducting economic forecasts, creating marketing strategies, and accounting for financial information are just 8a few responsibilities of a small business owner. Above all, accounting plays an important role in small business management,helping track financial information for business functions.

**Facts**

Strong accounting systems may be the difference between creating a successful small business and filing for bankruptcy. The Small Business Administration (SBA) reports that two-thirds of new businesses survive for at least two years and only 44 percent last four years. Bradstreet company, reports that the main reasons small businesses fail are because of poor capital structure, overspending when starting a business, lack of cash reserves, and poor accounting controls.

**Features**

Small business use a mix of management or financial accounting with business operations. Management accounting focuses on the allocation of business costs to goods or services, creating budgets for business functions, and preparing financial information for business decisions. Financial accounting prepares financial statement listing sales revenues, expenses,assets,liabilities,and cash flow for the small business, both types are used to secure external financing or report financial performance to business stakeholders.

**Function**

Accounting information allows business owners to assess the efficiency and effectiveness of their business operations. Prepared financial statements can be compared to industry standardsor to a leading competitor to determine how the small business is doing. Business owners may also use historical financial accounting statements to create trends for analyzing and forecasting future sales.

**Considerations**

Small business owners can purchase accounting software computer programs to track, record, and report financial information. While small or home-based small business can use spreadsheets or other basic programs to track financial information, specialized accounting software helps business owners maintain accurate financial records. Computerized accounting systems can compute payroll taxes for employee, too.

**Expert Insight**

Business owners may consider hiring a public accounting firm or individual certified public accountant (CPA) to create or review a company’s accounting system. Hiring a public accountant is often expensive for many small businesses. However, the experience and expertise public accountants bring to analyzing small business accounting may be an invaluable resource for running a business. Small business owners may also ‘us these outside accountants to prepare business tax returns.

**QUESTION 2: What is the different between accounts payable and accounts receivable? (20 Marks)**

How a transaction is recorded in the General Ledger (GL) depends upon the nature of the transaction. **Accounts Payable** (AP) is recorded in the AP sub-ledger when an invoice is approved for transactions where the company must pay to vendors for the purchase services or goods. On the other hand, **Account Receivable** (AR) records any money that a company is owned because of the sale of their goods or services. On the company’s balance sheet, accounts payable are recorded as liabilities while receivables are recorded as assets.

**Comparison chart**

|  |  |  |
| --- | --- | --- |
| **Differences** | **Account Payable** | **Account Receivable** |
| **Refers to** | Money that the company owes to others. | Money that others owe to the company. |
| **Abbreviation** | A/P or AP | A/R or AR |
| **Paid to whom?** | Accounts payable are amounts a company owes because it purchased goods or services on credit from a supplier or vendor. | Accounts receivables are amounts a company has a right to collect because it sold goods or services on credit to a customer. |
| **Recorded as** | Liability (payable always a liability) | Asset (receivables always an assets) |
| **How each affects a business?** | Accounts payable will decrease a company’s cash. | Accounts receivable will increase a company’s cash. |
| **What causes this transaction?** | Purchasing goods on credit. | Selling goods on credit. |

**Execution**

Accounts payable is recorded when an invoice is approved for payment. Many companies use “segregation of duties,” i.e. making sure no single employee can approve a payment alone, to prevent embezzlement.

For most businesses, accounts receivable involves the generation of an invoice, which is delivered to the customer. The customer must than pay the invoice within the payment terms, usually within 30 days.

**Working capital Management.**

Working capital (WC) represents the operating liquidity of a business. Net working capital is the difference between current assets and current liabilities. It is important of companies to have a healthy, positive net working capital. This is achieved through, among other techniques, astute management of accounts payable and receivables.

Accounts receivables are analyzed by the average number of days to collect payment ( called Days Sales Outstanding or DSO), and accounts payable are analyzed by the average number of days it takes to pay an invoice (Days Payable Outstanding or DPO).

DSO = Accounts Receivable

Average sales / day

DPO = Accounts Payable

COGS / day

Where COGS is cost of goods sold and COGS / day is the daily average of purchases.

DSO of less than 45 days is generally considered healthy.

Working capital can be increased by reducing the DSO or increasing the DPO i.e. collecting payment from customers quicker and delaying payments to vendors. However, there is always a business trade-off because payment to vendors could tarnish the company’s reputation and could also result in missing out on early payment discounts. Similarly, customers may be more willing to offer business if the company is not too strict about getting paid on time.

**Special Uses**

Accounts receivable can be used as collateral when obtaining a loan. They can also be sold in capital markets.

**QUESTION 3: Why does a company’s profit appear as a credit on its balance sheet? (20 Marks)**

**Introduction to balance sheet.**

The accounting balance sheet is one of the major financial statements used by accountants and business owners. (The other major financial statements are the income statement, statement of cash flows, and statements of stockholders equity) The balance sheet is also referred to as the statement of financial position.

The balance sheet presents a company’s financial position at the end of a specified date. Some describe the balance sheet as a ‘snapshot’ of the company’s financial position at a point (a moment or an instant) in time. For example, the amounts reported on a balance sheet dated December 31, 2016 reflect that instant when all the transactions though December 31 have been recorded.

Because the balance sheet informs the reader of a company’s financial position as of one moment in time, in allows someone- like a creditor-to see what a company owns as well as what it owes to other parties as of the date indicated in the heading. This is valuable information to the banker who wants to determine whether or not a company qualifies for additional credit or loans. Other who would be interested in the balance sheet include current investors, potential investors, company management, suppliers, some customers, competitors, government agencies, and labor unions.

**Assets**

Assets are things that the company owns. They are the resources of the company that have been acquired through transactions, and have future economic value that can be measured and expressed in dollars. Assets also include coast paid in advance that have not yet expired, such as prepaid advertising, prepaid insurance, prepaid legal fees, and prepaid rent. Example of assets accounts that are reported on a company’s balance sheet include:

* Cash
* Land
* Land improvements
* Buildings
* Supplies
* Petty cash

**Liabilities**

Liabilities are obligations of the company; they are amounts awed to creditors for a past transactions and they usually have the word “payable” in their account title. Along with owner’s equity, liabilities can be thought of as a source of the company’s assets. They can also be thought of as a claim against a company’s assets. For example, a company’s balance sheet reports assets of $100 000 and Accounts Payable of $40,000 and owner’s equity of $60,000. the source of the company’s assets are creditors/suppliers for $40,000 and the owners for $60,000. The creditors/suppliers have a claim against the company’s assets and the owner can claim what remains after the Accounts Payable have been paid.

Liabilities also include amounts received in advance for future services. Since the amount received (recorded as the asset Cash) hes not yet been earned, the company defers the reporting of revenues and instead reports a liability such as Unearned Revenues or Customer Deposits. Example of liability accounts reported on a company’s balance sheet include:

\* Notes Payable

\* Accounts Payable

\* Income Taxes Payable

\* Customer Deposits

\* Warranty Liability

**Accounting Equation**

What is the Accounting Equation? The equation that is the foundation of double entry accounting. The accounting equation displays that all assets are either financed by borrowing money or playing with the money of the company’s shareholders. Thus, the accounting equation is: Assets= Liabilities + shareholder Equity. The balance sheet is a complex display of this equation, showing that the total assets of a company are equal to the total of liabilities and shareholder equity.

**Double Entry**

What is double entry? Double entry is the fundamental concept underlying present-day booking and accounting. Double-entry accounting is based on the fact that every financial transaction has equal and opposite effects in at least two different accounts. It is used to satisfy the equation Assets= Liabilities + Equity, in which each entry is recorded to maintain the relationship.

The fundamental concept of double entry derives from the use of debit and credit to record business transaction. The total debits always equal the total credits. Customarily, in bookkeeping and accounting, the assets, expense and loss accounts are listed on the left side of a bookkeeping sheet, and the liability, equity, revenue and gain accounts are listed on the right side, with the two sides maintaining the same total balance. A debit to one or more accounts must be accompanied by a credit to at least one account, equally increasing or decreasing the balance on each side. Other times, a debit to either side is balanced out by an equal credit to the same side.

**Example of balance sheet:**

**Dr**   **Cr**

**Non-current Assets**   **$ Equity and capital $**

Land and building xxx Capital xxx

Vehicles xx net profit

Machinery xx net loss xx

Equipment xx xxxx

xxxx Drawings (-) xx

xxx

**Current Assets Current Liability**

Stocks xx Creditor xx

Cash xx

Bank xx **Non-current liability**

Debtor xx Bank loan xx

Xxxx xxxx

**Why does a company’s profit appear as a credit in its balance sheet?**

The accounting equation and the double entry system provide an explanation why a company’s profit appears as a credit in its balance sheet.

Asset accounts usually have debit balance while liabilities and owner’s or stockholders equity usually have credit balances. When a company provides services for cash, its assets Cash is increased by a debit and its owner’s equity is increased by a credit. The credit is initially recorded in a revenue account, but revenue accounts are temporary accounts that cause owner’s equity to increase.

If the owner withdraws some cash for personal use, the asset cash will decrease through a credit and the owner’s equity will decrease through the debit part of the accounting entry. The debit might initially be recorded in the sole proprietor’s Drawing account but this account is also a temporary account that will cause the owner’s equity to decrease.

Generally speaking, the credit balance reported in the owner’s or stockholders equity section of the balance sheet reflects the owners investments in the company plus the profits earned minus the amounts distributed to the owners since the time that the company began.

**QUESTION 4: What is meant by reconciling an account? (20 Marks)**

Reconciling an account often mean proving or documenting that an account balance is correct. For example, we reconcile the balance in the general ledger account Cash in Checking to the balance shown on the bank statement. The objective id to report the correct amount in the general ledger account Cash and checking. You will often need to adjust the general ledger account balance for items appearing on the bank statement that were no entered in the general ledger account.

I recall being asked to reconcile the general ledger account Freight Payable. What I needed to do was provide documentation that the balance in Freight Payable was proper. I proceeded to look at the shipments of recent sales and then determined how much we would be obligated to pay for the freight on those sales. We then adjusted the balance in Freight Payable to my documented amount. This reconciliation was done to have the correct account balance and to provide the outside auditors be reviewed.

I also reconciled the balance in Utilities Payable by computing the daily cost of each utility that the company used. The cost per day was then multiplied by the number of the days since the last meter reading date shown on the utility bills already entered in our accounting system. We then adjusted the utilities payable account balance to be equal to the documented amount.

**What does Reconcile mean in Accounting Terms?**

Reconciling financial accounts with your accounting records will help you identify errors, irregularities and needed adjustments. In accounting, reconcile means to compare two sets of records to make sure they are in agreement. One of those sets of records is usually a bank account or other type of financial account, and the other set of records is usually your accounting records.

**Reconciliations**

Bank reconciliations are the most common type of reconciliation. To ensure accurate accounting records, perform reconciliations on all your financial accounts. Compare each transaction in your financial statement with the same transaction in your accounting records. As you complete your reconciliation, you will add some entries such as fees, interest income or interest expense entries from the financial statement to your accounting records. Check the transactions off as you verify them as proof the transactions have cleared the financial institution. Most accounting software have a built-in way for you to perform a reconciliation and check off each cleared transaction. Accounting paper and check registers also have a column you can check off as you reconcile your account.

**Catch mistakes**

A reconciliation tells you which transactions have cleared the financial institution. As you perform your reconciliation, you may encounter transactions that seems to match but with different amounts. The best way to determine whether you or the financial institution has made a mistake is to examine the original financial record. You should still have this record at the time of the reconciliation, because according to the IRS, you should keep financial record backups such as bills, receipts and deposits for a minimum of three years. If the mistake is yours, correct your mistake. If the financial institution made the mistake, call and work with it to correct your account.

**Find Fraud**

To protect your company from worker fraud, have a person who does not input financial transactions perform reconciliations. Reconciliations sometimes reveal entries in the financial statement that are not in your accounting records. First investigate in-house to determine if the entry is legitimate. If you cannot find a legitimate source for the entry in-house, call the financial institution and ask for clarity. If the transaction is fraudulent, get your financial institution to remove it if possible. Another type of fraud easily detected through a reconciliation is check fraud. A reconciliation will flush out transactions where a person alters a check you have given him or writes a check on your account without your permission.

**Security Measures**

Reconciliations will also let you know which transactions you have entered that the bank has not yet processed. These are called deposits in transit and outstanding checks. If you made a deposit at the end of the statement period and it is not on the statement, this is normal; it will appear on the next statement. However, if you make a deposit at the beginning of the statement period and it does not appear in the statement, this is something you should investigate. Unlike unprocessed deposits, unprocessed checks are rarely a sign of fraud. It usually means someone has forgotten to deposit the check in his account. If the check stays unprocessed for many months, call the recipient as a courtesy to remind her to deposit the check.

**CONCLUTION**

In this part, I understanding what is business accounting actually and business accounting consists of three basic activities: identifying, recording and communicating the economic events of a company. Accountants identify economic events such as transactions and investments. Accountants use bookkeeping techniques to systematically record economic events. Finally, accountants use financial statements to present their records to people who use accounting information. Sometimes, accounting might also mean analyzing and interpreting financial statements and explaining the meaning of reported data.

I also learn how business accounting is important by analyzing income and expenses, which gives an overall in the business financial health and also what is bookkeeping is, which is more focused on recording business activity and producing documentation of transactions. Moreover, I study about business accountants manage and produce financial statements, pay taxes for the company, and oversee all necessary financial reporting via internal or outsource to accounting firms. In other hand, I also learn about the double entry system and balance sheet.

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