

Name: Ruben Goh Sen Lee

Login ID: ruben@oasis-portal.com

Course Title: Accounting Fundamentals

Subject Code: BHM03

Submitted date: 8/8/2017

**Table of Contents**

|  |  |  |
| --- | --- | --- |
| **No** | **Details** | **Page** |
| 1 | Executive Summary | 3 |
| 2 | Introduction | 4 |
| 3 | Assignment Question |  |
|  | Part 1 | 5-8 |
|  | Part 2 | 9-12 |
|  | Part 3 | 13-14 |
|  | Part 4 | 15-16 |
| 4 | Conclusion | 17 |
| 5 | References | 18 |
|  | Appendix |  |

**Executive Summary**

In this assignment, I will be explaining about the fundamentals of accounting. Accounting is needed in every company to keep track of records and its progress and to show whether the company is gaining or losing profits. In the first part, a brief and detailed explanation will be given on the role of accounting. In the second part, an elaboration will be given explaining the difference between accounts payable and accounts receivable. In the third part, a brief clarification will be given as to explain why a company's profit appears as a credit on the balance sheet. In the final part, a detailed explanation will be given on reconciling an account.

**Introduction**

Accounting is the recording of financial transactions which includes storing, sorting, retrieving, summarizing, and presenting the information in various reports and analyses. Accounting is also a profession consisting of individuals having the formal education to carry out these tasks. Accounting also require providing a company's management with the information it needs to keep the business financially healthy. These analyses and reports are not distributed outside of the company. Some of the information will originate from the recorded transactions but some of the information will be estimates and projections based on various assumptions. Three examples of internal analyses and reports are budgets, standards for controlling operations, and estimating selling prices for quoting new jobs. This area of accounting is known as management accounting.

**Assignment Questions**

**Question 1**

In a brief but comprehensive response, define the role of accounting.

The role of accounting in business is to help internal and external stakeholders make better business decisions by providing with financial information. Accounting relays information that owners, managers, and investors need to assess a company's financial performance so as to make better judgements. Accounting is done by two types of accountants that works in two types of major fields such as management accounting, which helps you keep your business running, or financial accounting, which tells you how well you're running it. The purpose of management accounting is to supply relevant, accurate, timely information to managers in a format that will aid them in making decisions that will bring positive results. The purpose of financial accounting is to provide information that helps with assessment in a firm's financial history and current performance and show ways of how to improve said performance.

Financial accounting includes:

**Income Statements**

A financial statement that reports a company's financial performance over a specific accounting period. Financial performance is assessed by giving a summary of how the business incurs its revenues and expenses through both operating and non-operating activities. It also shows the net profit or loss incurred over a specific accounting period.

Unlike the balance sheet, which covers one moment in time, the income statement provides performance information about a time period. It begins with sales and works its way down to net income and earnings per share (EPS).

The income statement is divided into two parts which are operating and non-operating. The operating part of the income statement discloses information about incomes and expenditures that are a direct result of regular business operations. For example, if a business creates sports wear, it should make money through the sale and/or production of sports wear. The non-operating section discloses income and expenditure information about activities that are not directly tied to a company's regular operations. Continuing with the same example, if the sports company sells real estate and investment securities, the gain from the sale is listed in the non-operating items section.

**Balance Sheets**

A financial statement that summarizes company's assets, liabilities and shareholders' equity at a specific point in time. These three balance sheet segments give investors an idea as to what the company owns and owes, as well as the amount invested by shareholders.

The balance sheet adheres to the following formula:

Assets=Liabilities + Shareholders' Equity

Assets

Accounts Receivable

Cash

Inventory

Investments

Building and Equipment

Liabilities

Loans

Accounts Payable

Salaries

Equity

Capital Stock

Retained Earnings

**Statement of Cash Flows**

Also known as cash flow statement, is a financial statement that shows how changes in balance sheet accounts and income affect cash and cash equivalents, and breaks the analysis down to operating, investing, and financial activities.

**Question 2**

What is the difference between accounts payable and accounts receivable?

Accounts Payable

An entity's obligation to pay off a [short-term debt](http://www.investopedia.com/terms/s/shorttermdebt.asp) to its creditors is presented by an accounting entry known as accounts payable also known as (AP) for short. On many [balance sheets](http://www.investopedia.com/terms/b/balancesheet.asp), the accounts payable entry appears under the heading [current liabilities](http://www.investopedia.com/terms/c/currentliabilities.asp). Another common usage of AP refers to a business department or division that is responsible for making payments owed by the company to suppliers and other creditors.

Accounts payable are debits that must be paid off within a given period to avoid [default](http://www.investopedia.com/terms/d/default2.asp). For example, at the corporate level, AP refers to short-term debt payments to suppliers. The payable is essentially a short-term [IOU](http://www.investopedia.com/terms/i/iou.asp) from the business to the other business, who acts as a [creditor](http://www.investopedia.com/terms/c/creditor.asp).

To record accounts payable, accountants or bookkeepers credit accounts payable when they owe a bill, and they debit accounts payable when they pay the bill. For example, imagine a business incurs a $700 invoice for office supplies. When the AP department receives the invoice or incurs the bill, it records it as a debit in an accounts payable field. As a result, if anyone looks at the total debit in the accounts payable category, he can instantly see what the business owes to all of its vendors and short-term lenders. When the bill is paid, the department enters a credit in its accounts payable column.

To balance these entries, the accountant must enter a debit in the relevant category, office supplies in this case, when the debt is incurred, and he must enter a credit in the cash column when he pays the invoice.

Accounts receivables and accounts payable are essentially opposites. Accounts payable is the money a company owes its vendors, while accounts receivables is the money that is owed to a company. If a company has a bill in its accounts payable department, the company it owes the funds to categorizes the bill in its accounts receivables department.

Accounts Receivable

Outstanding invoices that a company has or the money the company is owed from its clients are referred to by accounts receivable. The phrase refers to accounts a business has a right to receive because it has delivered a product or service. [Receivables](http://www.investopedia.com/terms/r/receivables.asp) essentially represent a [line of credit](http://www.investopedia.com/terms/l/lineofcredit.asp) extended by a company and due within a relatively short time period, ranging from a few days to a year.  
Most companies operate by allowing some part of their sales to be on credit. In some cases, business offer this type of credit to frequent or special customers who are invoiced periodically. The practice allows customers to avoid the hassle of physically making payments as each transaction occurs. In other cases, businesses routinely offer all of their clients the ability to pay after receiving the service. For example, electric companies typically bill their clients after the clients have received the electricity. While the electricity company waits for its customers to pay their bills, the unpaid invoices are considered accounts receivable.  
If a company cannot collect its accounts receivable, it may decide to take the debtor to court over the unpaid debt, or it may outsource the debt collection activity to a third-party bill collector. These companies typically charge a set fee or a percentage of the amount they collect. In other cases, businesses sell their accounts receivable for pennies on the dollar to a factoring company that then collects the debt. Factoring companies often offer some cash up front, making them an attractive option for companies that need a boost to their working capital.

If a business has reported an account receivable as income and it does not receive payment, it has a bad debt. The Internal Revenue Service (IRS) allows businesses to subtract bad debts from their gross income on their income tax returns, as long as they reported the debt as income on a previous return.

When a company owes [debts](http://www.investopedia.com/terms/d/debt.asp) to its suppliers or other parties, these are known as [accounts payable](http://www.investopedia.com/terms/a/accountspayable.asp). Accounts payable are the opposite of accounts receivable. To illustrate, imagine company A cleans company B's carpets and sends a bill for the services. Company B owes the money, so it records the invoice in its accounts payable column. Company A is waiting to receive the money, so it records the bill in its accounts receivable column.

**Question 3**

Why does a company's profit appear as a credit on its balance sheet??

The [accounting equation](https://www.accountingcoach.com/blog/accounting-equation) and the [double entry system](https://www.accountingcoach.com/blog/what-is-the-double-entry-system) provide a detailed explanation on why a company's profit appears as a credit on its balance sheet.  
  
Liabilities and owner's or [stockholders' equity](https://www.accountingcoach.com/blog/what-is-stockholders-equity) usually have [credit balances](https://www.accountingcoach.com/blog/what-is-a-credit-balance) while asset accounts usually have [debit balances](https://www.accountingcoach.com/blog/what-is-a-debit-balance). When a company provides services in exchange for cash, its asset cash is increased by a debit and its [owner's equity](https://www.accountingcoach.com/blog/what-is-owners-equity) is also increased by a credit. The credit is initially recorded in an income account, but income accounts are [temporary accounts](https://www.accountingcoach.com/blog/what-is-a-temporary-account) 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](https://www.accountingcoach.com/blog/what-is-an-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?

Reconciliation is an accounting process that uses two different sets of records to ensure figures are explicit and in agreement. Reconciliation is the key process used to determine whether the money leaving an account matches the amount spent, ensuring that the two values are balanced at the end of the daily, monthly or annual recording period.

There is no benchmark method of accounting reconciliation, but generally accepted accounting principles (GAAP for short) considers the double-entry accounting and account conversion to be the main forms of reconciliation, and businesses and individuals may reconcile their records daily, monthly or annually using either of these methods.

At the end of every month, many individuals usually reconcile their [checkbooks](http://www.investopedia.com/terms/c/checkbook.asp) and [credit card](http://www.investopedia.com/terms/c/creditcard.asp) accounts by comparing their canceled checks, [debit card](http://www.investopedia.com/terms/d/debitcard.asp) receipts and credit card receipts with their bank and credit card statements. This type of account reconciliation makes it possible to determine whether money is being fraudulently withdrawn. It also ensures that [financial institutions](http://www.investopedia.com/terms/f/financialinstitution.asp) have not made any errors with individuals' accounts, and it gives individual consumers an overall picture of their spending.

When an account is reconciled, the statement's transactions and ending balance should match the account holder's records. For a [checking account](http://www.investopedia.com/terms/c/checkingaccount.asp), it is also important to know how any pending deposits or checks outstanding affect the statement balance.

Account [reconciliation](http://www.investopedia.com/video/play/reconciliation-0/) is also important for businesses. Businesses must reconcile their accounts to check for fraud and to prevent [balance sheet](http://www.investopedia.com/terms/b/balancesheet.asp) errors. Businesses typically uses [accounting software](http://www.investopedia.com/terms/a/accounting-software.asp) to help them perform account reconciliations. Mistakes can have serious ramifications for publicly traded companies. For example, an [auditor](http://www.investopedia.com/terms/a/auditor.asp) who reviews the company’s [financial statements](http://www.investopedia.com/terms/f/financial-statements.asp) in accordance with federal regulations such as the Sarbanes-Oxley Act could find a material error, which the company would have to publicly disclose as a failure of controls, a material misstatement and/or a material weakness. Without accurate financial information, a company will not be able to make well-informed decisions.

**Conclusion**

In my opinion, accounting is an important aspect in every business as it keeps track of and records all movements and records made by the company and informs the owners' of any errors if any are found. It is safe to say that because of accounting, any business decisions will be made with careful planning and expenditure to ensure a step forward towards any goal of a company.

**References**

Retrieved from [**https://www.boundless.com/accounting/textbooks/boundless-accounting-textbook/introduction-to-accounting-1/overview-of-key-elements-of-the-business-19/the-role-of-accounting-in-the-business-119-7274/**](https://www.boundless.com/accounting/textbooks/boundless-accounting-textbook/introduction-to-accounting-1/overview-of-key-elements-of-the-business-19/the-role-of-accounting-in-the-business-119-7274/)

Investopedia (2017)(online) [**http://www.investopedia.com/terms/i/incomestatement.asp**](http://www.investopedia.com/terms/i/incomestatement.asp)

Wikipedia (2017)(online) Retrieved from <https://en.wikipedia.org/wiki/Cash_flow_statement>

Investopedia(2017)(online) Retrieved from <http://www.investopedia.com/terms/b/balancesheet.asp>

Investopedia(2017)(online) Retrieved from <http://www.investopedia.com/terms/r/reconciliation.asp>

THE END