

Name: Kong Loke Yee

Login ID: konglokeyee@oasis-portal.com

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**Executive Summary**

In this module, I covered the topic about the theory and basic knowledge of Accounting Fundamentals. In starting part, we can see the role of accounting which means the users of accounting data. What is accounting and what is role of accounting? In the first part, I studied the different between accounts payable and accounts receivable and will explain debtor and creditor belongs to which “family”. In the second part, I will describe why does company profit appear as credit on its balance sheet and I will brief the balance sheet, accounting equation, trading profit and loss. In the final part, I will define the bank reconciliation statement and explain the purpose and importance of reconciling an account. Apart from this, I also brief about the difference between cash book and bank statement.

**Introduction**

This explanation of accounting basics will introduce you to some basic accounting principles, accounting concepts, and accounting terminology. Once you become familiar with some of these terms and concepts, you will feel comfortable navigating through the explanations, quizzes, puzzles, and other features of AccountingCoach.com.

Some of the basic accounting terms that you will learn include revenues, expenses, assets, liabilities, income statement, balance sheet, and statement of cash flows. You will become familiar with accounting debits and credits as we show you how to record transactions. You will also see why two basic accounting principles, the revenue recognition principle and the matching principle, assure that a company's income statement reports a company's profitability.

Accounting can seem like a daunting discipline for a small business owner. When you discuss accounting, you'll hear a lot of complex terms. It helps to begin with fundamental accounting. All advanced accounting depends on the fundamental equation that defines every business's success or failure.

Identification involves observing economic events and determining which of those events represent economic activities relevant to a particular business. Selling goods to a customers, paying wages to employees and providing services to a client are examples of economic activities. Economic events of an entity are referred to by accountants as transaction, and are of two types, external and internal. Accountants use the single term transaction to refer to both internal and external transaction. Transaction constitute the inputs of the accounting information syatem.

**Question 1**

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

Accounting is one of the main function of the organization and also a system of recording the financial Transaction of the business. It is a process of summarizing (getting money information), analyzing (checking) and reporting financial transaction. Accounting is all about Debit and Credit.

The history of accounting is thousands of years old and can be traced toancient civilizations.The early development accounting dates back to ancient Mesopotamia, and it is closely related to developments in writing, counting money and early auditing systems by the ancient Egpytians and Babylonians. By the time of the Emperor Edrian Henio, the Roman government had access to detailed financial information. The Father of accounting – Luca Pacioli created Double Entry which contents Debit and Credit in T-ledger. Debit was represent the left side and Credit was represent the right side of T-ledger.

Debit has to record expenses of owner such as rental, utilities, salary, discount given and so on. Therefore, Debit has also to record asset. There is two type of asset, non-current asset and current asset. Non-current asset means that the asset can be last more than one year such as land and building, vehicles, machineries, equipment and so on. Current asset means that the asset can be last within one year only, such as cash in hand, cash in bank, stock or inventory, debtor and so on.

Credit has to record all income of owner such as rental received, commission received, discount received and so many. Besides, Credit has also to record liability. Same as asset, liability also divided into two type, non-current liability and current liability. Non-current liability is a long-term debt which the duration of liability more than one year, such as bank loan, mortgage and so on. Instead, current liability is a short-term debt means the duration of liability less than one year, such as creditor, bank overdraft, credit card and so many.

The role of accounting for a good manager plans for the future. They also develop a budget which is a formal plan stated in monetary terms. Accounting help bank decide to lend money for a person because the balance sheet will show their sales, purchases, net profit, assets and everything about the person who would like to borrow money from bank. Accounting provides information that helps investors pick stock. The role of accounting basically budgeting, information systems design, cost counting and internal auditing.

Accounting information is useful to anyone who makes decisions that have economic results.   
Owners want to know which employees are productive.  
Investors want to know if a company is good investment.  
Legislators want to know how a proposed law will affect budgets.  
Managers want to know if a new product will be profitable.  
Creditors want to know if they should extend credit, how much to extend and for how long.  
The role of accounting in business is to help internal and external stakeholders make better business decisions by providing them with financial information.

**Question 2**

**What is the difference between accounts payable and accounts receivable?**

|  |  |
| --- | --- |
| Accounts payable | Accounts Receivable |
| Accounts payable is a debtor. Debtor is someone who buy our products. When we sell our products to debtor, money in. Its form our income. | Accounts receivable is a creditor. Creditor is someone we buy products from. When we buy our products from creditor, money out. Its form our expenses. |
| An short term current liability. Presents in Income Statement under sales category. | An short term current asset.Presents in Balance Sheet under short term assets |
| Example: Sold goods on credit $800 | Example: bought goods on credit $500 |
| Determines profitability of the business | Determines fluidity of the business |
| Calculates for a specific period time. (Example: monthly/annual credit sales) | An accumulative value, This value represents total due of customers as at a particular date. |

**Question 3**

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

Balance sheet is a statement of the assets, liabilities, and equity of a business or other organization at a particular point in time. A balance sheet is based on simple accounting equation which is [Asset = liability + equity] or [Equity = assets - liabilities].

|  |  |
| --- | --- |
|  | Liability |
|  | Equity and Capitals  Capitals xxxxx  (+)net profit@(-)net loss xxxxx  xxxxx  (-)drawings xxxxx  Current Liability  Account payable xxxxx  Bank overdraft xxxxx  Non-current Liability  Bank loan xxxxx |

Every transaction that happens within a business has an effect on its financial position. The accounting equation is what keeps all of the transaction in balance and helps users of the information make sense of what areas each transaction affects. The financial position of any company is based on the following items:  
Assets: what the company owns  
Liabilities: what the company owes  
Equity: difference between assets and liabilities

Trading Account is transacting medium to buy and sell shares. A trading account is similar to a traditional bank account, holding cash and securities, and is administered by an investment dealer. A profit and loss statement (P&L) is a financial statement that summarizes the revenues, costs and expenses incurred during a specific period of time, usually a fiscal quarter or year. These records provide information about a company's ability – or lack thereof – to generate profit by increasing revenue, reducing costs, or both. The P&L statement is also referred to as "statement of profit and loss", "income statement," "statement of operations," "statement of financial results," and "income and expense statement."

Profit is determined by the money you get from sales, cost of stock (if you sell product/s) and of course all the expenses you incur. Keeping a close eye on each of these will ensure you are maximising the profit in your business.To calculate the profit in your business you need to know that:

-sales consist of commissions paid / discounts given + cost of goods + gross profit

-gross profit is made up of variable + fixed expenses + net profit.

Sales, gross profit and net profit are the income earned by the business.

Cost of goods, commissions/discounts, variable and fixed expenses are business expenses.

A profit and loss statement shows planned and actual profit for your business. Our Financial statements template includes a profit and loss statement

**Question 4**

**What is meant by reconciling an account?**

As indicated before, the Cash at Bank account balance at a particular date rarely agree with the balance shown on a bank statement of the same date. To prove the accuracy of both records it is necessary to compare them, identify factors that have caused a variation in the balances, and satisfy oneself that if these factors are taken into account the two sets of record agree. This process is referred to as reconciling the bank’s balance as disclosed on the bank statement to the balance shown in the Cash at Bank account of the depositor. For effective control, this process should be carried out at least once a month .To formalize this process of reconciliation, a special statement called a bank reconciliation statement is prepared.

The reconciliation process is concerned with identifying the transactions and entries that cause the balances in the Cash at Bank account and the bank statement to differ at a particular date.

The difference between the bank statement and cash books consist of outstanding checks, deposits in transit, bank service charges, check printing charges, errors on the books, errors by the bank, electronic charges on the bank statement not yet recorded on the books, and electronic deposits on the bank statement that are not yet recorded on the books. In cash book, a debit bank balance indicates an asset but in the bank statement, a debit balance indicates a bank overdraft (we owe money to the bank – an asset for the bank) in our cash book, a credit bank balance indicates a liability (overdraft) but in the bank statement, a credit balance indicates a positive balance (the bank owes us money)

Bank Reconciliation Statement as at……..

Balance as per bank statement Cr (or Dr) xxxx

Add (or deducted) outstanding deposits xxxx

xxxx

Deduct (or add) unpresented cheques xxxx

Balance as per Cash at Bank account (Dr or Cr) xxxx

**Conclusion**

Accounting is service activity. Its function is to provide and interpret information that is intended to be useful in making economic decisions. Business entities, government departments, charitable organization and not-for-profit organizations, family units and individuals all engage in economic activity which involves making decisions about allocating available resources effectively. People need relevant information to be able to make sound economic decisions.

Accounting is often called the ‘language of business’ . A language is means of social communication and involves a flow of information from one person to one or more other people. Everyone involves in business, from the beginning employee to the top manager, eventually uses accounting information in the decision-making-process. To be effective, the receiver of the information must understand the message that the sender intends to convey. Accounting uses its own special words and symbols to communicate information that is intended to be useful for economic decision making by managers, shareholders, creditors and many other.

The importance of understanding accounting information is not restricted to those engaged directly in business. Many people with little knowledge of accounting must interpret accounting data. For example, lawyers must often understand the meaning of accounting information if they are to represent their clients effectively, marketing consultants must be aware of the costs of developing advertising campaigns, and engineers and architects must consider cost data when designing new equipment and buildings.

**References**

(Information from another source must be credited in the reference page)

Example:

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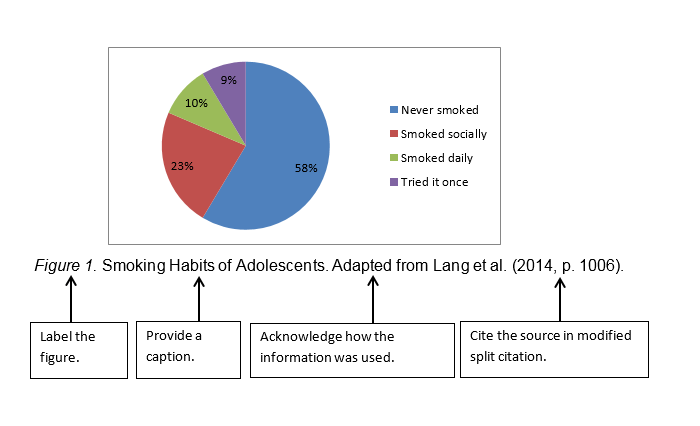
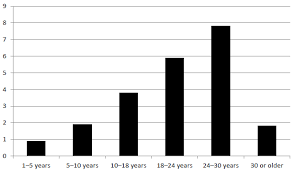
* Difference between cash book and bank statement

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**Appendix**

(Appendix is for more detailed information on a subject that is too long to explain in 1 page)

Example:



THE END