accounting VS BOOKEEPING

↳ Interpretation of the Financial Statements (from bookkeeper)
- Involves collecting, recording, classifying and interpreting the Financial Data

↳ maintains records of the Financial Statement / Transaction
- Ensures that they are up to date and accurate.

PROCESS of BOOKKEEPING

Transaction ⟶ Business Document ⟶ Books of
Trial Balance ⟵ Ledgers ⟵ Prime Entry

BUSINESS DOCUMENTS

↳ Invoice
- By Seller : Demand for payment (only when buying / selling goods on credit)
↳ Debit Note
- By Customer : Request reduction in invoice
↳ Credit Note
- By seller : Accept reduction in invoice
↳ Cheque
- By customer : Payment of amount
↳ Receipt
- By seller : Acknowledgement of payment
↳ Statement of accounts
- By seller : To summarise transaction

BOOK of PRIME ENTRY

↳ Journals
- General / Purchases / P.R / Sales / S.R (Goods on credit)
↳ Cash book
- Normal / Petty cash (on cash / bank)

LEDGERS

↳ Every individual account from Journals
- Total for the month (TFTM) posted only

TRIAL BALANCE

↳ Debit
- Asset, Expenses

↳ Credit
- Revenue, Liability

A C C O U N T I N G
principles

Realisation
↳ The revenue is recognised as being earned when ownership of goods passes to customer.

Prudence
↳ Asset and profit should NOT be overstated

Matching
↳ Cost and Expenses should be matched against REVENUE

Duality
↳ Every transaction has a 2 fold aspect.

Money Measurement
↳ Transaction must be expressed in monetary terms

Business Entity
↳ Financial Transaction of business must be seperate from owner

Going Concern
↳ Financial Statement assumes business will continue to operate indefinately

Materiality
↳ Purchases of small amounts should not be written as NCA but be written off in the year
   as they are incurred

Consistency
↳ The SAME accounting treatment must be applied to similar items at all times
  ⇒ To ensure Income Statement and SOFP can be compared meaningfully

Historic Cost
↳ Transactions recorded at cost price to the business

DEPRECIATION

↳ Estimated lost in value of NCA over its expected working life

Purpose :

↳ To spread the cost of NCA over its useful life

↳ To comply with (matching principle) [all cost should be matched with revenue]

Why depreciation has to be provided for in the Final Accounts of the business?

↳ To provide for wear and tear of the assets used during operations.

↳ To calculate profit and loss accurately

↳ To ensure matching principle is applied

⇒ Better allocation of costs against revenue

Causes of depreciation :

① Physical detioration [wear and tear]

② Economic reasons [technology / growth in company]

③ Passage of time [outdated - lose value]

④ Depletion

M E T H O D S

Straight line :

Cost of asset × percentage

= ??? [Fixed for all years]

Advantages:

↳ Simple to understand and easy to calculate

↳ Depreciates evenly

↳ Helps to estimate amount of depreciation in advance

Disadvantages :

↳ Equal amount charged every year although capacity / efficiency declines

↳ Does not consider seasonal flunctuations in the use of fixed assets

Reducing - balance :

Net book value × percentage = ???

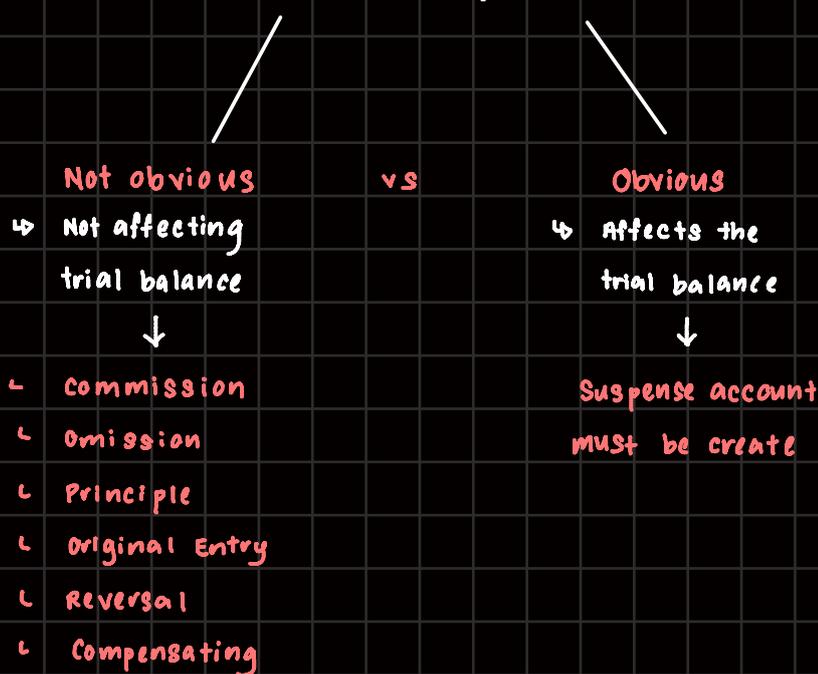↳ Cost of asset - accumalated depreciation

Advantages :

↳ Same percentage written off every year

↳ Higher % charged in early years where machine is most efficient

Disadvantages :

↳ more complicated

↳ Takes very long to write off assets unless a high rate of depreciation is used

ERRORS
and suspense

Not obvious   vs   **Obvious**

↳ Not affecting   ↳ Affects the
    trial balance   trial balance

      ↓   ↓

   └ Commission   Suspense account
   └ Omission   MUST be create
   └ Principle
   └ Original Entry
   └ Reversal
   └ Compensating

Omission
↳ Completely omitted (missed) from books

Commission
↳ Wrong account, SAME class

Principle
↳ Wrong account, WRONG class

Original Entry
↳ Wrong figure / amount

Reversal
↳ Debit instead of credit (vice versa)

Compensating
↳ 2 or more errors cancel each other out

Transposition *
↳ 2 numbers are reversed
(eg. 450 → 405)

BANK RECONCILIATION STATEMENT

Ⴑ Purpose : To explain the difference between the bank statement and cash book

+	Cash Book (A)	-
Uncredited	Unpresented	
Cheques received	cheques issued	

Paired with →

-	Bank Statement (L)	+
		Bank interest

Prepared by the business owner

Ⴑ Both uncredited/presented cheques are recorded in cash book but not yet recorded in bank statement

* cash book may need to be at the end of the year due to difference in bank statement [make comparison]

Prepared by the banker

Ⴑ Unpresented/credited cheques might not appear here due to timing difference when creating these accounts + diff ppl create

* Banker might +/- from account without informing business owner (eg. bank interest) Thus, it needs to be updated in cash book

2 methods

Balance as per cash book	×××
(+) unpresented	××
(-) uncredited	(××)
Balance as per bank statement	×××

OR

Balance as per bank statement	×××
(+) uncredited	××
(-) unpresented	(××)
Balance as per cash book	×××

Why is the bank statement balance is opposite to the bank account show in cash book ?

Ⴑ The bank statement is a COPY of the bank account of the business but in the books (eyes) of the bank

   - Prepared in viewpoint of the bank (banker)

Partnership

Partnership agreement

(E) Interest on capital
(E) Partners Salary
(E) Sales Commission
(R) Interest on Drawings

] Recorded in current & appropriation accounts

Purpose :
To avoid disagreements or misunderstanding in the partnership.

Appropriation account [IAS]

Profit for the year	XX	
Interest on drawings	XX	XXX
		XXXX
(-) Appropriation		
Partners Salary	XX	
Interest on Capital	XX	
Sales Commission	XX	(XXX)
Profit/Loss Shared		± XXXX

- Current Account (L) +

Drawings	XX	XX	Int. On Capital	XX	XX
Int. on drawings	XX	XX	Sales Comm	XX	XX
			Salaries	XX	XX
	XX	XX		XX	XX

Alternate presentation in SOFP [next page →]

ADVANTAGES   VS   DISADVANTAGES

ADVANTAGES	DISADVANTAGES
↳ Access additional capital	↳ Profits shared
↳ Share loss / risk	↳ Disagreements
↳ Share responsibilities	↳ Greater responsibility
↳ Additional ideas	↳ Harder decision making

Reasons partner may make a loan instead of additional capital ?

↳ Greater security
↳ Repaid before capital in winding up

Why interest on capital received ?

↳ Rewards for :
- Business investments
- Lost oppurtunity cost of capital involved

Advantages
∟ To partner : Rewarded for investing
∟ To partnership : Encourages each partner to invest in the business

Why interest on drawings charged ?

↳ To limit partners drawings
↳ Ensure enough cash is retain in business

Advantages
∟ To partners : Reduces Drawings
∟ To partnership :
- Prevent partner from taking out cash from business , causing cash flow problems
- Discourages large / early cash withdrawels
= Improve cash / working position

Current Account in [SOFP]

NCA

-
-

CA

-
-

Capital and Liabilities	Person 1	Person 2	Total
Capital Account	xx	xx	xxxx
Current Accounts			
Balance b/d [Date]	xx	xx	
Interest on Capital	xx	xx	
Partners Salary	xx	xx	
Profit shared	xx	xx	
	xxx	xxx	
(-) Drawings	xx	xx	
Interest on drawings	xx	xx	
Loss shared	xx	xx	
	(xxx)	(xxx)	
	xxxx	xxxx	xxxxx
			xxxx

Either profit or loss shared

manufacturing accounts

⤷ To calculate how much it has cost the business to manufacture the goods produced in the Financial Year

Raw Materials

⤷ Goods remaining (at the end of the year) which were purchased for converting into Finished Goods

Work in Progress

⤷ Goods which are partly made (at the end of the year)

⤷ Items of production which are partially completed

Direct cost / Expenses

Factory Overhead

⤷ INDIRECT factory expenses

- Cannot be easily traced to the product manufactured.

* SOFP of manufacturing business follows the same format except there may be 3 inventories

Eg. Current Asset

Inventory - Material	xxx
- Finished goods	xxx
- Work in progress	xxx

CLUB
Non-profit organisations

Accumalated Fund = Asset - Liabilities

↳ Equivalent to **Capital** in a trading organisation

↳ Annual surplus (w/o deficit) accumalated

Income and Expenditure → NOT income statement

↳ Non monetary items

↳ Includes adjustment for accrued/prepaid

income statement

Trading

Revenue (Sales)

to

Gross Profit

Profit and Loss

Gross Profit

to

PFTY

Income and Expenditure

↳ Use PFTY from income statement
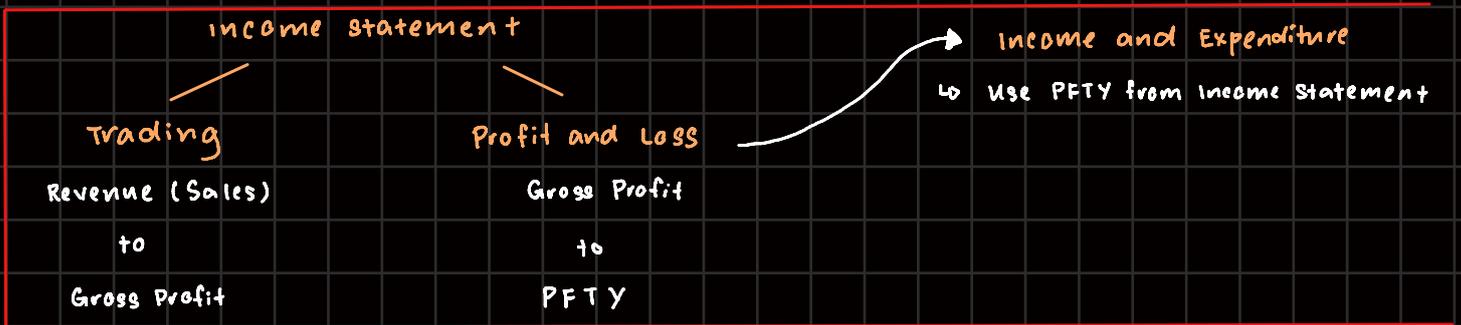
Ask teacher

COMPANY

SOLE TRADER

ADVANTAGES

- ↳ Few legal regulations
- ↳ His own boss : full control
- ↳ Freedom to make own decisions
- ↳ Receive all profits

DISADVANTAGES

- ↳ Unlimited liability *
- ↳ Limited source of finance
- ↳ No continuity of business after death

Limited Liability :
- ↳ Members only lose what they invested

Unlimited liability :
- ↳ If business cannot pay debts , the owner has to pay from personal belonging

LIMITED COMPANY

- ↳ Owners of companies : Shareholders [members of one company]
  - ⇒ Jointly owned by ppl that has invested in it

2 Types of shareholders

∟ Private limited companies

- – Owned by family / friends
- – They invest capital and run the business
- – Shares cannot be sold / transferred w/o agreement of others

∟ Public limited companies

- – Shares offered to public and its traded on stock exchange
- – conduct by directors

* All Shareholders have limited liabity

Shareholders own company
Directors controls company

Share Capital

Preference sharep ca ital

- – Receive FIXED RATE of dividend
- – Not entitled to vote in shareholders AGM
- – Receive dividend of profit b4 ordinary share dividend
  - ∟ Higher Priority
- – Receive capital before ordinary shareholders
  [In event company is closed]

Ordinary share Capital

- – Receive VARIABLE dividends
- – Be entitled to vote in AGM
  - ↳ one vote per share
- – Receive dividend of profit after ordinary share dividend
- – Last one to receive capital if company closes

Dividends : Paid to shareholders (like a reward for investment)
  ↳ From profits of company

Authorised share capital
└ Maximum amount of shares a company is allowed to sell

Issued share capital
└ Amount of shares actually issued / sold

Called-up capital
└ Total amount of money asked for from its preference and ordinary shareholders

Paid-up capital
└ Part of called-up capital where money has actually been received from its preference and ordinary shareholders

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Profit for the year (100%)

General Reserve (50%   Dividends (20%)

Retained Earnings
(30%)
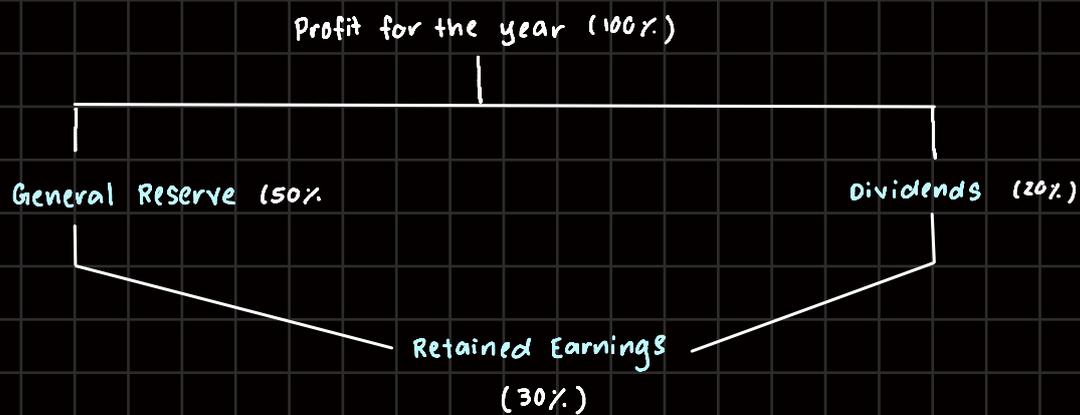
Statement of changes in equity....

	Share Cap	General. R	Retained Profits	Total
Bal at 1 Jan 2020	xxx			xxx
PFTY			xxx	xxx
Transfer to General.R		xxx	(xxx)	0
Dividend paid			(xxx)	(xxx)
Bal at 31 Dec 2020	xxx	xxx	xx	xxx

SOFP extract.....

Equity and Liabilities	
Equity and Reserves	
Share Capital	xxx
General Reserve	xxx
Retained Profits	xxx
Shareholders fund	xxx

accounting
R A T I O

PROFITABILITY

① Gross margin $\dfrac{GP}{Sales} \times 100\%$

② Profit margin $\dfrac{PFTY}{Sales} \times 100\%$

③ Mark-up $\dfrac{GP}{COS} \times 100\%$

④ Return on Capital Employed

[ROC] $\dfrac{PFTY}{Capital} \times 100\%$ ↳ Owner's Equity + NCL

[ROCE] $\dfrac{Profit\ b4\ loan\ interest}{Capital\ Employed}$

Working capital = CA - CL

LIQUIDITY

① Current Ratio $\dfrac{CA}{CL}$ → Ratio of 2:1 is ideal

② Liquid / Quick Ratio $\dfrac{CA - Inventory}{CL}$

↳ Acid test ↳ Ratio of 1:1 is ideal

③ Rate of inventory turnover

$\dfrac{COS}{Avg\ Inventory}$ = No. of times

To find number of days :

$\dfrac{365\ days}{No.\ of\ times}$ OR $\dfrac{Avg\ inventory}{COS} \times 365\ days$

④ Trade Receivable Turnover

$\dfrac{TR}{Credit\ Sales} \times 365\ days$ = No. of days

⑤ Trade Payable Turnover

$\dfrac{TP}{Credit\ Purchases} \times 365\ days$ = No. of days