

Module 1.

Developing a Viable Business

Adramé Ndione



Agenda

Session 1 : Founding ground for a viable business

- Defining Investment readiness
- Business Strategy
 - Industry Analysis
 - Market Analysis

Session 2 : Analyzing your key differentiators

- Key resources and capabilities
- A business Model that creates value

Session 3: Strategy execution for a leadership positioning

- Operational excellence: Developing your operations
- Developing customer intimacy: Marketing and sales

Session 4: Understanding your finances

- Bookkeeping
- Financial Statements

Session 5: Budgeting and forecasting

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SESSION 4: UNDERSTANDING YOUR FINANCES

- Bookkeeping and accounting
- Financial Statements

Agenda

- Bookkeeping & Accounting
 1. Role of bookkeeping & accounting
 2. The bookkeeping process
 3. Case studies
- Financial Statements

Session structure

Session organization

Section	Activity	Time allocation
First quarter	Opening & Energizer	10mn
Second quarter	Learning	60mn
Third quarter	Application or learning	40mn
Fourth quarter	Wrap up & session evaluation	10mn



Key objectives

- Understand the accounting process and have the tools necessary to maintain a sound accounting system.
- Be able to make management decisions based on reliable financial figures.

Session 4

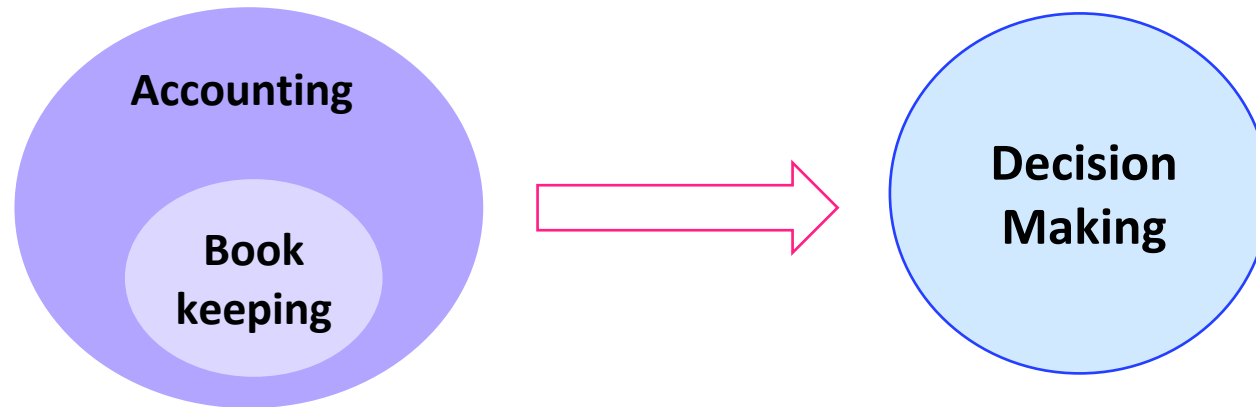
Understanding your finances

- **Bookkeeping and accounting**
 1. **Role of bookkeeping & accounting**
 2. The bookkeeping process
 3. Case studies
- Financial Statements



Bookkeeping vs. Accounting

- Bookkeeping – the process of recording all information regarding the transactions and financial activities of a business.
- Accounting – preparing reports based on the information accumulated by the bookkeeping process to enable decision making



What is bookkeeping?

Book-keeping is simply keeping the records of business transactions.

Examples of transactions:

- sale/ purchases of goods/ services;
- Income;
- Payments by an individual or organization.

- You have £10.
- Your mother/father/aunt gives you £100 because today is your birthday.
- You go with your friends to celebrate your birthday.
- You have £15 left after the celebration.
- How much money did you spend?
- *In businesses, **all** of this would be **recorded** !*

What is Good Bookkeeping?

- Tracking income and expenses;
- Tracking debts and investments;
- Monitoring net worth and cash flow;
- Ensure that you can meet your tax requirements and liabilities;
- Reduce the cost of annual accounting fees;
- Reduce the risk of a tax audit;
- Provides efficient cash flow report;
- Ability to see where money is being spent.

Why is “Bookkeeping” important?

- The only way to really know and understand what is going on financially is to track income and expenses carefully.
- After the end of the year, the benefits of having taken time to keep books becomes evident.
- History is one of the best predictors and is very useful in establishing a meaningful and helpful budget.

What is Accounting?

- **Providing** financial information in an organization to enable management to perform three functions:
 - Recording;
 - Analysis;
 - Control.
- **Using** financial information to analyze the performance of management of (and inside) an organization
 - Objectively;
 - Consistently;
 - Professionally;
 - With reliable techniques for internal management control;
 - and comparing overall performance of the organization with other organizations.
- **Obtaining** finance (capital) for management of an organization
- **Forecasting** management/departmental/organizational performance
- **Checking** actual performance against planned/ forecasted performance
- **Auditing** claims (claimed performance) of organizations
- etc.

Who Needs Accounting?

- Managers use accounting information in making investment decisions;
- Investors use accounting information in valuing stocks;
- Bankers rely in accounting information in deciding whether to lend money to a business and in assessing the risk of the loan;
- Accounting information is crucial in evaluating the performance of employees at various levels in an organization.
- ...

Financial Accounting Vs. Managerial Accounting

Accounting is sometimes called “**the language of business**” used by investors, creditors, governmental agencies, and others.

There are 2 broad types of accounting information: **Financial Accounting & Managerial Accounting**

Financial Accounting

- Provides information primarily to people outside the company
- Provides information that would be helpful in attracting capital
 - Equity and debt (useful in debt contracts);
 - Credit from suppliers;
 - Customers;
 - Employees.
- Provides information helpful in monitoring and evaluating management performance

Managerial Accounting

- Provides information to people inside the company
 - Internal investment decisions
 - Performance evaluation

Financial Accounting Vs. Managerial Accounting



	Financial Accounting	Management Accounting
Prepared for	External user groups	Internal user groups
Purpose	Satisfy information needs of External users	Assist managerial decision making, planning and control
Level of detail	Summarized or aggregated at organizational level	Detailed and specific information on parts of the organizations operations
Frequency of information	Usually annual accounts	As required by managers
Time horizon	The past, i.e. historical	The future plus past information used for control purposes
Constraints on content	Normally, legal requirements and accounting standards influence the content and format of financial statements	None – content can be tailor made to meet managerial requirements

International accounting standards: IFRS & GAAP

Accounting standards, are guidelines and regulations issued by governing bodies. They dictate how a company records its finances, how it presents its financial statements, and how it accounts for things such as inventories, depreciation, and amortization. (Investopedia)

1. Regularity
2. Consistency
3. Sincerity
4. Performance of Methods
5. Non-compensation
6. Prudence
7. Continuity
8. Periodicity
9. Full Disclosure/ Materiality

International Financial Reporting Standards (IFRS)

IFRS has become the global standard for the preparation of public company financial statements.

Fifteen of the G20 countries have adopted IFRS. China, India, and Indonesia have national accounting standards that are similar to IFRS, while Japan allows companies to follow the standards voluntarily

Generally Accepted Accounting Principles (GAAP)

GAAP is the standard adopted by the Securities and Exchange Commission (SEC) in the U.S. Except for foreign companies, all companies that are publicly traded must adhere to the GAAP system of accounting

Basic Accounting Terms

- Assets
- Income
- Creditors
- Stock / Inventory
- Profit
- Drawings
- Liabilities
- Expenditure
- Goods / work- in-process
- Purchase
- Voucher
- Capital
- Revenue
- Cost
- Sales / Discount
- Expenses
- Debtor
- Gain
- Loss
- Transaction
- Credit
- Depreciation
- Solvent
- Book Value
- Entry
- Receivables
- Bad debts
- Debit
- Payable
- Insolvent

Basic Accounting Terms

- Account – a record of activities in a categories.
- General ledger – complete set of accounts created and maintained by a business.
- Chart of account – formal index of accounts.

Single-entry system Vs. Double-entry system

Single-entry bookkeeping system

Single-entry bookkeeping uses only income and expense accounts, recorded primarily in a revenue and expense journal.

Klein Company Three-Column Record June 20YY		
Date	Transaction	Amount
1 June 20YY	Starting balance for the day	\$4,520.00
1 June 20YY	Electricity bill for the month	(\$149.80)
2 June 20YY	Postage stamps purchased	(\$43.00)
2 June 20YY	Inventory purchased	(\$624.15)
3 June 20YY	Daily product sales	\$1,040.25
3 June 20YY	Sales tax paid	(\$83.22)
4 June 20YY	Daily service revenues	\$592.25
4 June 20YY	Bank interest received	\$180.83
5 June 20YY	Customer refund paid	(\$42.95)
5 June 20YY	Ending balance for the day	\$5,390.21

Double-entry bookkeeping system.

Double-entry bookkeeping requires recording each transaction twice, using debits and credits.

Particulars	Debit	Credit
B Limited A/c	\$2,500	
Cash A/c		\$2,500

Particulars	Debit	Credit
Machinery A/c	\$30,000	
Cash A/c		\$30,000

Particulars	Debit	Credit
Cash A/c	\$1,500	
Rent Received A/c		\$1,500



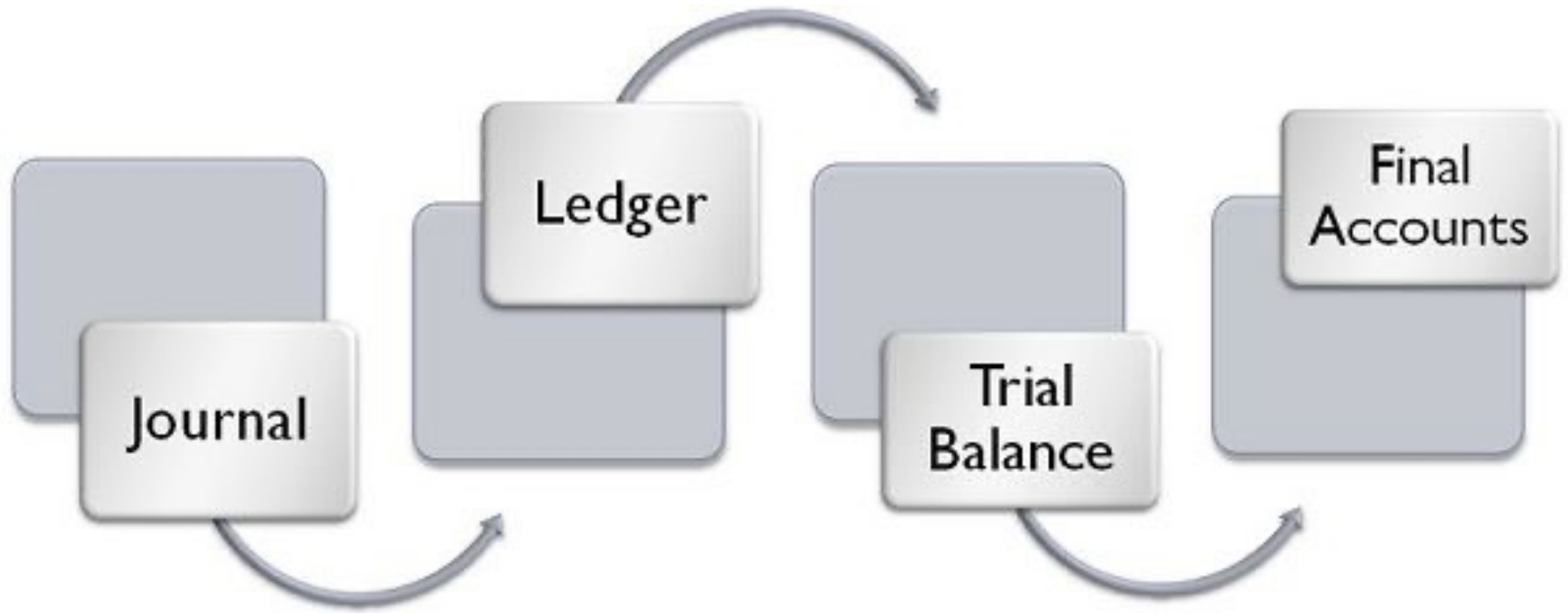
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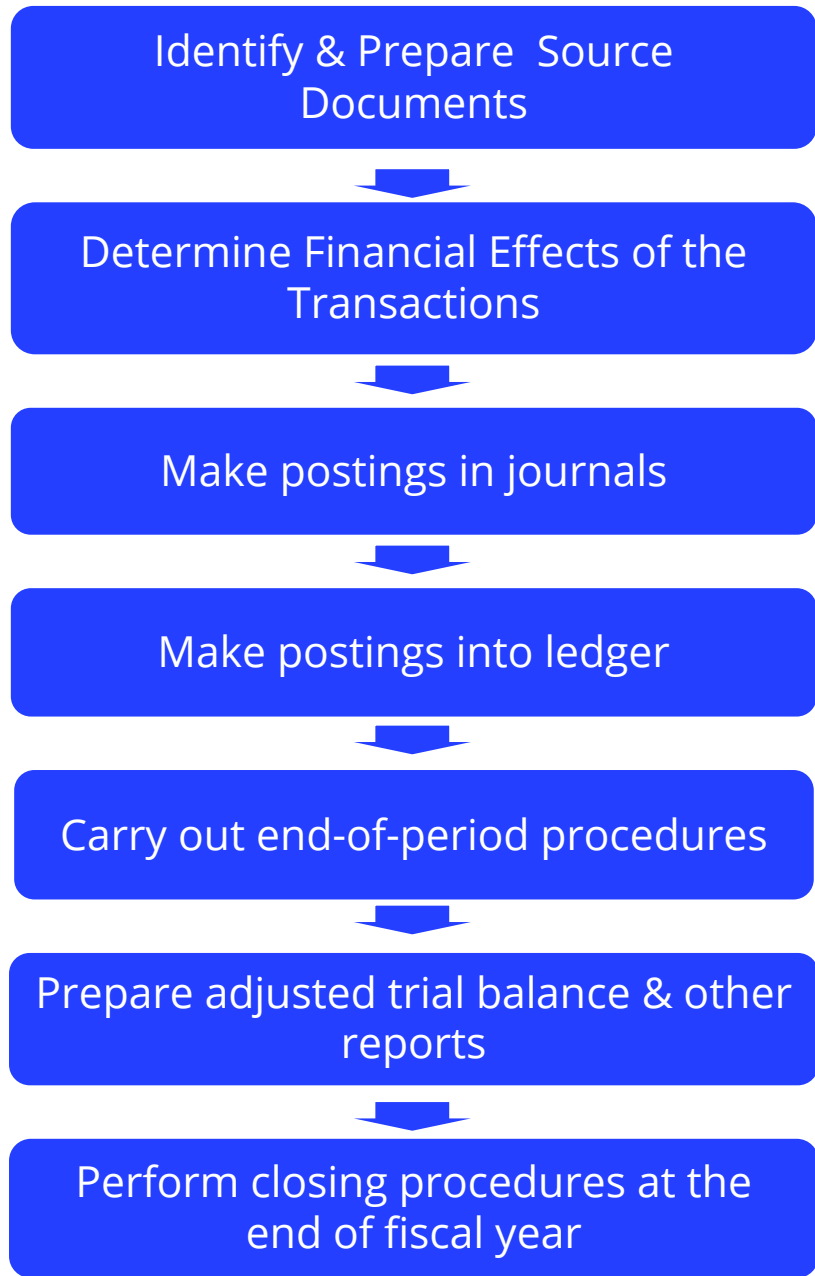


From Journal to Final accounts/ financial statements





Bookkeeping Process



Sources of Documents

What information should be covered in the documents?



Sources of Documents

Income

- Sales Invoices (including tax invoices)
- Sale vouchers or receipts
- Cash register tapes, credit card statements
- Bank Deposit Books and Bank Statements
- Loan Agreements

Expenses

- Purchase invoices (including tax invoices)
- Receipts
- Cheque Butts
- Credit Card Statements
- Bank Statements
- Loan Agreements

Sources of Documents

Record to keep for employee:

- Tax file number declaration;
- Worker payment records;
- Payment Summaries;
- Annual Reports;
- Superannuation records;
- Records of any Fringe Benefits provided;
- Time Sheets.

Record relating to business payments:

- Records of amounts withheld from payment;
- Copy of PAYG Withholding Voluntary Agreement;
- Records of Voluntary Payments;
- PAYG Payment Summaries;
- Annual Reports.

Recording your transactions

Invoice

- Check all invoices including tax invoices.

Purchases

- If you use cheques, make sure you record enough information on the cheque butt—date, payee, details of goods and amount.

Journal and Ledger

Journal

A Journal is that primary books of accounts in which transactions are originally recorded in a chronological order. i.e. as they occur

Date	Particulars	Ledger Folio	Dr. (Amt)	Cr. (Amt)
2009 May 5	Cash A/C.. To Mr.MM (Being cash received from MM)	53 page of cash Book 37 page of MM A/C	2,500	2,500

Ledger

From Journals, transactions are posted in the Ledger. Ledger, as the second stage books of accounts, serves as the basis for preparing Trial Balance & final accounts.

<u>Dr</u>				<u>Cr</u>			
Date	Particulars	LF	Amt	Date	Particulars	LF	Amt.

Distinction between Journal and Ledger

JOURNAL

- It is a book of primary entry
- Primary documents such as vouchers , are the basis for recording transactions in the Journal
- Recording in the Journal is the first stage
- All transactions are recorded in chronological order in Journal
- Journal will have five columns:
(i) Date (ii) Particulars (iii) Ledger Folio (iv) Debit Amt. (v) Credit Amt.
- Journal is not balanced
- The process of recording in journal is called journalizing
- Journal by itself does not serve as the basis for preparing final accounts

LEDGER

- It is book of final entry
- Journal is the basis for recording transactions in the ledger
- Recording in the Ledger is the second stage
- It is prepared to see the net effect of various transactions affecting a particular account
- Ledger has four identical columns on debit and credit sides (i) Date, (ii) Particulars, (iii) Folio, (iv) Amount
- All ledger accounts (except nominal A/c) are balanced in the ledger
- The process of recording in the ledger is called posting
- Ledger serves as the basis for the preparation of final accounts

Journals

- Journals is used to record the daily details of transactions.
- The raw data is posted in summarized to ledger accounts
- Thus, journals are used to group together transactions of similar nature to make postings to the ledger accounts easier.

Date	Transaction Code	Supplier/Customer	Description	CoA	Account Name	Debit	Credit
						Balance	
1/24/2017	R-092	S003	Purchase Return 1 Unit Mobile Phone C	2110	A/P - Trade	369.33	
1/24/2017	R-092	S003	Purchase Return 1 Unit Mobile Phone C	5300	Purchase Discounts - All Products	59.25	
1/24/2017	R-092	S003	Purchase Return 1 Unit Mobile Phone C	5400	Purchase Returns and Allowances - All Products		395.00
1/24/2017	R-092	S003	Purchase Return 1 Unit Mobile Phone C	2130	VAT - Input		33.58
1/25/2017	R-870	C005	Sales Return	4300	Sales Returns and Allowances - All Products	790.00	
1/25/2017	R-870	C005	Sales Return	2140	VAT - Output	71.10	
1/25/2017	R-870	C005	Sales Return	1250	Account Receivables		782.10
1/25/2017	R-870	C005	Sales Return	4200	Sales Discounts - All Products		79.00

Journal

A Journal contains day-to-day transactions in a chronological order. It records both the debit and credit aspects of a transaction by using Double Entry System of Bookkeeping

FORM of JOURNAL

<u>(1) Date</u>	<u>(2) Particulars</u>	<u>(3) Ledger Folio</u>	<u>(4) Dr. (Amt)</u>	<u>(5) Cr.(Amt)</u>
XXXX	XXXXXXXXXXXXXX	XXXX	XXXX	XXXX

Rules for Making Journal Entries

<u>Type of Account</u>	<u>Debit</u>	<u>Credit</u>
1. Personal Account	The Receiver	The Giver
2. Real Account	What comes in	What goes out
3. Nominal Account	Expense & Losses	Incomes & gains

Special Journals

Small businesses often uses the following journals:

1. Cash receipt journal;
2. Cash payment journal;
3. Credit sales journal;
4. Credit purchase journal;
5. General journal.

Cash Receipt Journal



Date	Account Cr.	Rec. No	Discount allowed	Customer	Cash Sales		Other Receipts	Amount Banked
					Cash sales	COGS		

Amount banked = customer + cash sales + other receipts – discount allowed

Cash Payment Journal

Date	Account Dr.	Chq. No	Discount Received	Supplier	Inventory Control	Other payments	Amount Paid

Amount paid = supplier + Inventory control + other payments – discount received

Credit Sales Journal



Date	Account Dr.	Post. Ref	Inv. no	Product 1		Product 2	
				COGS	Revenue	COGS	Revenue

Credit Purchase Journal



Date	Supplier	Inv. No	Prod 1	Prod 2	Total

General Journal



Date	Accounts	Post Ref.	Debit	Credit

Important Journal Entries: **EXERCISE & SOLUTIONS**

From the following transactions, pass Journal Entries

Transactions (EXERCISE)

1. Cash brought into business as Capital

2. Cash and other assets brought into business

3. Goods purchased on credit

4. Sale of goods on credit

5. Goods purchased on cash / by cheque

Journal Entries: (SOLUTIONS)

Cash / Bank A/c Dr.
To Capital A/c Cr.

Building A/c Dr.
Plant & machinery A/c Dr.
Cash A/c Dr.
To Capital A/c Cr.

Purchase A/c Dr.
To supplier A/c Cr.

Customer A/c Dr.
To Sales A/c Cr.

Purchase A/c Dr.
To Cash/bank A/c Cr.

Important Journal Entries (contd.) **EXERCISE & SOLUTIONS**

From the following transactions, pass Journal Entries

Transactions (EXERCISE)

6. Cash sales

7. Bad debts

8. Purchase of machinery for cash

9. Depreciation charged on assets

10. Goods returned by the customer

Journal Entries: (SOLUTIONS)

Cash A/c Dr.
To Sales A/c Cr.

Bad debts A/c Dr.
To Customer A/c Cr.

Machinery A/c Dr.
To Cash/bank A/c Cr.

Depreciation A/c Dr.
To Asset A/c Cr.

Returns inward A/c Dr.
To Customer A/c Cr.

Ledger Account

The number and types of ledger are determined by the nature and volume of business. The main Ledgers (Books) required to be maintained for running an SME enterprise will be:

- Cash Book;
- Purchase Book;
- Purchase Return Book;
- Sales Book;
- Sales Return Book;
- Bills Receivable Book;
- Bills Payable Book.

General Ledger Summary

Demo Company (Global)
From 1 June 2021 to 30 June 2021

[Add Summary](#)

Account	Debit	Credit	Net Movement
Accounts Payable (800)	1,592.60	7,756.26	(6,163.66)
Accounts Receivable (610)	2,248.18	0.00	2,248.18
Advertising (400)	2,309.47	0.00	2,309.47
Business Bank Account (090)	0.00	1,592.60	(1,592.60)
Computer Equipment (720)	1,969.99	0.00	1,969.99
Consulting & Accounting (412)	29.00	0.00	29.00
Freight & Courier (425)	115.50	10.00	105.50
General Expenses (429)	120.09	0.00	120.09
Inventory (630)	320.00	320.00	0.00
Light, Power, Heating (445)	100.32	0.00	100.32
Motor Vehicle Expenses (449)	380.00	0.00	380.00
Office Expenses (453)	107.11	0.00	107.11
Purchases (300)	775.98	0.00	775.98
Rent (469)	1,091.22	0.00	1,091.22
Sales (200)	0.00	2,067.60	(2,067.60)
Sales Tax (820)	599.97	170.58	429.39
Telephone & Internet (489)	50.00	0.00	50.00
Travel - National (493)	223.56	0.00	223.56
Unpaid Expense Claims (801)	0.00	115.95	(115.95)
Total	12,032.99	12,032.99	0.00

[Export detailed General Ledger to Excel](#)

General Ledger Account

Account Name:

Date	(Balance) Account	Debit	Credit	Balance

Common Practices

- Recording of monthly sales;
- Recording of income and expenses;
- Recording of inventory;
- Routine financial reporting;
- Budgeting financial reporting;
- Budgeting planning;
- Debt and Account Receivables recording;
- Bank account recording.

Trial Balance

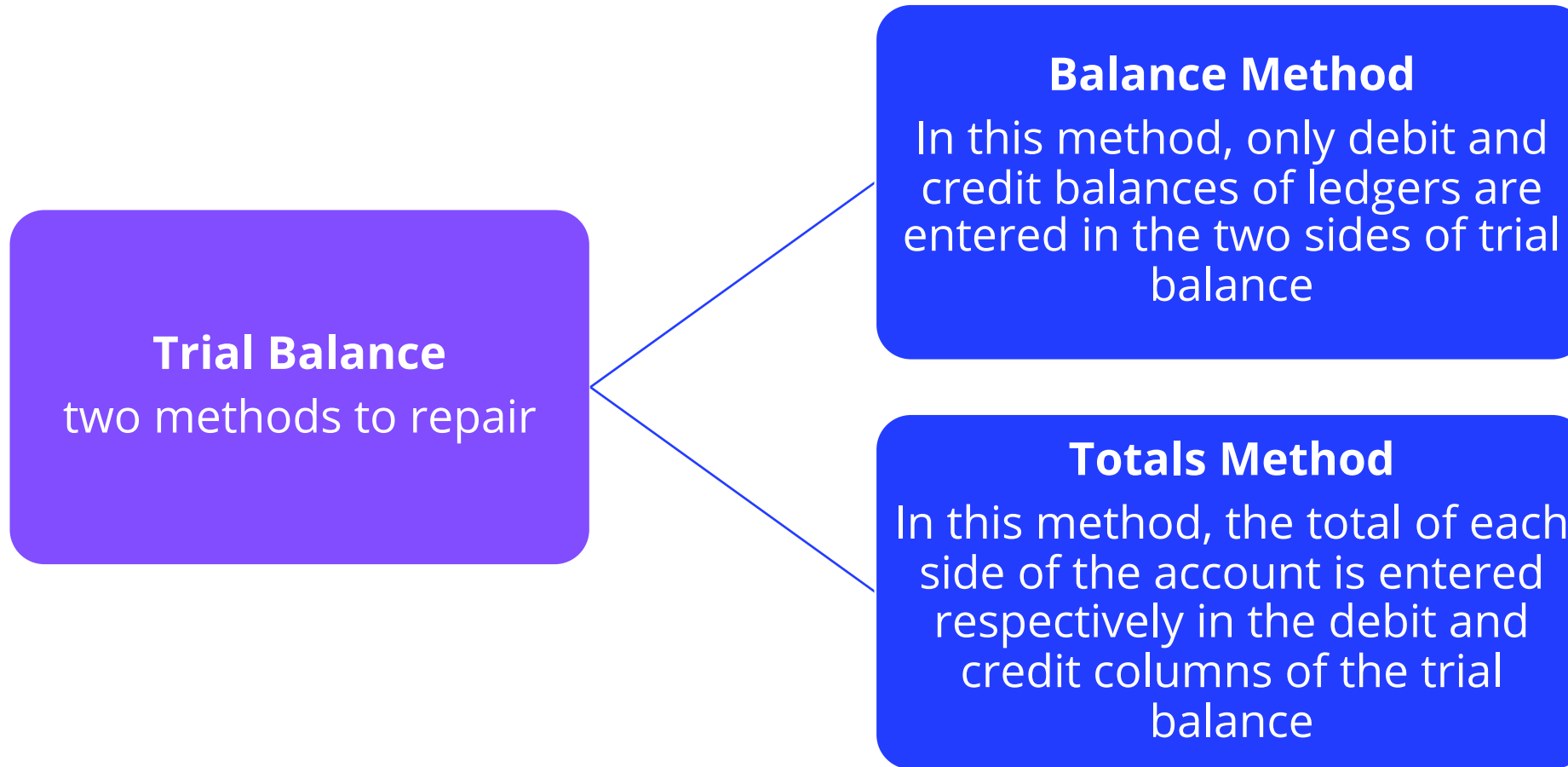
Definition

Trial Balance is a statement, prepared with the debit and credit balances of the ledger accounts including the balances of cash and bank taken from the Cash Book, to test the arithmetical accuracy of the books of accounts. Trial Balance serves as base for preparing the financial statements in an accurate manner.

Characteristics

- It is a list of balances of all ledger accounts and Cash Book.
- All ledger accounts showing debit balances are posted in one column and those showing credit balances are posted in the other.
- The total of debit balances in different accounts in the ledger must be equal to the total of credit balances in different accounts i.e. the totals of the two columns of the Trial Balance should agree
- If they agree, it means that both the aspects of each transaction have been correctly recorded in the ledgers
- It shows arithmetical accuracy of posting of entries from Journal to Ledgers.
- **Debit balances:** Assets, drawings, debtors, expenses, & Losses
- **Credit balances:** Liabilities, capital, creditors, incomes, & gains

Trial Balance (contd.)



Ledger to Trial balance

A	B	C	D	E
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Trial Balance

Demo Company (Global)

As at 31 May 2021

Account Code	Account	Account Type	Debit	Credit
200	Sales	Revenue		20,905.58
400	Advertising	Expense	7,347.58	
404	Bank Fees	Expense	30.00	
408	Cleaning	Expense	110.00	
412	Consulting & Accounting	Expense	58.00	
420	Entertainment	Expense	1,553.60	
429	General Expenses	Expense	46.19	
445	Light, Power, Heating	Expense	235.50	
449	Motor Vehicle Expenses	Expense	274.36	
453	Office Expenses	Expense	705.48	
461	Printing & Stationery	Expense	94.41	
469	Rent	Expense	2,182.44	
473	Repairs and Maintenance	Expense	1,896.70	
489	Telephone & Internet	Expense	84.75	
493	Travel - National	Expense	32.24	
090	Business Bank Account	Bank	3,353.14	
610	Accounts Receivable	Current Asset	6,946.33	
710	Office Equipment	Fixed Asset	923.79	
720	Computer Equipment	Fixed Asset	1,804.50	
800	Accounts Payable	Current Liability		2,223.10
820	Sales Tax	Current Liability		419.35
840	Historical Adjustment	Current Liability		4,130.98
Total			27,679.01	27,679.01

A	B	C	D	E	F
General Ledger Report					
Demo Company (Global)					
From 1 January 2021 to 31 May 2021					
Date	Type	Transaction	Reference	Debit	Credit
Office Expenses (453)					
20.04.2021	PAY	Woolworths Market - Misc kitchen supplies for office		\$60.23	
29.04.2021	INV	Net Connect - Network diagnostics software	9781	\$500.00	
30.04.2021	INV	Swanston Security - Our share building doorman/security	AP	\$55.00	
6.05.2021	CN	PC Complete - Unable to supply DVD writer for laptop - backorder	OG laptop		\$250.00
6.05.2021	CN	Swanston Security - Refund as agreed	Refund		\$23.50
11.05.2021	INV	PC Complete - DVD writer for laptop	OG laptop	\$250.00	
21.05.2021	PAY	Woolworths Market - Misc kitchen supplies for office		\$31.50	
21.05.2021	PAY	Orlena Greenville		\$27.25	
31.05.2021	INV	Swanston Security - Our share building doorman/security	AP	\$55.00	
44347		Total Office Expenses (453)		\$978.98	\$273.50
		Net movement		\$705.48	

Trial Balance (contd.) Exercise & Solution

Date	Particulars	L.F.	Dr.	Cr.
1 Jan	Cash To capital		80,000	80,000
5 Feb	Purchase To Cash		25,000	25,000
20 Feb	Cash To Sales		30,000	30,000
25 May	Mr. RR To Sales		20,000	20,000
15 Jun	Ms. SS To cash		18,000	18,000
28 Jun	Cash To Mr. RR		20,000	20,000
2 Aug	Purchases To Cash		19,000	19,000
29 Aug	Drawings To Cash		1,500	1,500
10 Oct	Purchase To Mr. DD		17,000	17,000
20 Nov	Mr. DD To Cash To Discount Received		17,000	16,800 200
31 Dec	Salaries To Cash		2,000	2,000
			267,500	267,500

Trial Balance (contd.) Solution

Trial Balance (Balance method) as at 31 Dec 2009

Heads of Account	L.F.	Dr.	Cr.
Capital			80,000
Cash		47,700	
Purchase		79,000	
Sales			50,000
Drawings		1,500	
Discount received			200
Salaries		2,000	
		130,200	130,200

Trial Balance (contd.) Solution

Trial Balance (Total Method) as at 31 Dec 2009

Heads of Account	L.F.	Dr.	Cr.
Capital			80,000
Cash		130,000	82,300(**)
Purchases		79,000	
Sales			50,000
Mr. SS		18,000	18,000
Mr. RR		20,000	20,000
Drawings		1,500	
Mr. DD		17,000	17,000
Discount received			200
Salaries		2,000	
		267,500	267,500

Notes:

- (**)** The amount of 82,300 is the total of the credit side of the Cash Account
- The total of debit and credit sides of the Trial Balance (267,500) is the same as the total of the debit and credit sides of the Journal

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Understanding your finances

- **Bookkeeping and accounting**
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Activity

- Each group can work on the case in the following slides.

Forms of a Ledger Account & Illustration

(a) Format : Following is the form of a Ledger folio:

Dr				Name of the Account (say Wages A/c)				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				

(b) **EXERCISE:** Post the entries from Journal to Ledger Folio

Post the following entries from Journal to the concerned Ledgers:

6 March 2009	Furniture A/c	Dr.	1,200
	To Mack Woods A/c		1,200

(c) **Solution:**

(1) **First Ledger will be Furniture A/c with following entries transferred from the Journal:**

Dr				Furniture A/c				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
6 March 09	To Mack A/c	10	1,200-								

(2) **Second Ledger folio will be Mack Woods A/c with entire transferred from the Journal:**

Dr				Mack Woods A/c				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
				6 March 09	By Furniture A/c	..	1,200				

EXERCISE & SOLUTION: How To Make Journal Entries & Postings in Ledgers

EXERCISE: Journalize the following entries as on 1.4.09 & post them in respective Ledgers

Cash in hand	20,000	Plant & machinery	50,000
Sundry debtors	60,000	Land & building	100,000
Stock of goods	40,000	Sundry creditors	100,000

SOLUTION:

SOLUTION:		JOURNAL		
<u>Date</u>	<u>Particulars</u>	<u>L.F.</u>	<u>Dr. (Amt.)</u>	<u>Cr. (Amt.)</u>
1.4.09	Cash A/c	Dr.	.....	20,000
	Sundry debtors	Dr.	.....	60,000
	Stock A/c	Dr.	.....	40,000
	Plant & machinery A/c	Dr.	.....	50,000
	Land & building A/c	Dr.	.....	100,000
	To Sundry Creditors	.....	100,000	
	To Capital A/c (see note)			170,000 (*)

Note(): The excess of assets over Liabilities is the Promoter's Capital and is credited to his Capital A/c (Amt: 170,000)*
(For Postings of the above Journal Entries- See next slides)

EXERCISE & SOLUTION : How To Make Journal Entries & Postings in Ledgers (contd.)

(1) Dr. Name of Ledger : CASH A/C Cr.

Date	Particulars	LF	Amt	Date	Particulars	LF	Amt
<u>1.4.09</u>	To Balance B/d		20,000				

(2) Dr. Name of Ledger : Sundry Debtor's A/c Cr.

Date	Particulars	LF	Amt	Date	Particulars	LF	Amt
<u>1.4.09</u>	To Balance B/d		60,000				

(3) Dr. Name of Ledger : STOCK A/c Cr.

Date	Particulars	LF	Amt	Date	Particulars	LF	Amt
<u>1.4.09</u>	To Balance B/d		40,000				

4) Dr. Name of Ledger : Plant & Machinery A/c Cr.

Date	Particulars	LF	Amt	Date	Particulars	LF	Amt
<u>1.4.09</u>	To Balance B/d		50,000				

EXERCISE & SOLUTION: How To Make Journal Entries & Postings in Ledgers (contd.)

(5) Dr. Name of Ledger : Land & Building A/c Cr.

<u>Date</u>	<u>Particulars</u>	<u>LF</u>	<u>Amt</u>	<u>Date</u>	<u>Particulars</u>	<u>LF</u>	<u>Amt</u>
<u>1.4.09</u>	To Balance B/d		100,000				

(6) Dr. Name of Ledger : SUNDRY CREDITOR's A/c Cr.

<u>Date</u>	<u>Particulars</u>	<u>LF</u>	<u>Amt</u>	<u>Date</u>	<u>Particulars</u>	<u>LF</u>	<u>Amt</u>
				<u>1.4.09</u>	By Balance b/d		100,000

(7) Dr. Name of Ledger : CAPITAL A/C Cr.

<u>Date</u>	<u>Particulars</u>	<u>LF</u>	<u>Amt</u>	<u>Date</u>	<u>Particulars</u>	<u>LF</u>	<u>Amt</u>
				<u>1.4.00</u>	By Balance b/d		170,000

Session 4

Understanding your finances

- Bookkeeping and accounting
 1. Role of bookkeeping & accounting
 2. The bookkeeping process
 3. Case studies
- **Financial Statements**



Final Accounts

Final Accounts mean the Financial Statements prepared consequent to the drawing of Trial Balance.

Final Accounts have two parts:

1. Income Statement (Trading and Profit & Loss A/c);
2. Balance Sheet

Format of Trading Account

Trading Account for a year ending 31 March 2009

Dr.		Cr.	
Particulars	Amount	Particulars	Amount
To opening Stock		By Sales	
To Purchase		Less return	
Less return			
To Direct expenses		By closing stock	
To Wages & Salaries		By Abnormal loss of stock	
To Freight inward		By Gross Loss transferred	
		To P&L A/c (**)	
To Carriage inward			
To Cartage inward			
To Gross Profit transferred to P/L A/c (**)			

Note: (**) Either Gross Profit or Gross Loss will appear.

Financial Statement: Income statement

- Income statement measures the “performance” of a company over a period of time.
- Revenues -- a measure of economic benefits generated by the sale of products or providing of services over a period of time.
- Expenses -- a measure of economic sacrifices incurred to “earn” the revenues of a given period.
- Examples of expenses – cost of inventory sold, salaries to employees, rent and lighting, advertising, ...
- Net Income = Revenues (-) Expenses

Format of Profit and Loss Account

Profit and Loss A/c for the year ending 31 March 2009

Dr.		Cr.	
Particulars	Amount	Particulars	Amount
To Gross Loss transferred from Trading A/c		By Gross Profit Transferred from Trading A/c..	
To Salaries		By Rent	
To Rent rates and taxes		By Discount received	
To Stationary and printing		By Commission earned	
To Postage and telegrams		By Interest	
To Audit fees		By bad debts recovered	
To legal charges		By Income from Investments	
To Telephone Expenses		By Dividends on shares	
To insurance premium		By Miscellaneous Revenue	
To Depreciation		By Income from any other sources	
To Interest		By NET LOSS (**) (Transf. to Capital A/c)	
To (all expenses, travel, commission Bk. Charges, office exp., estab. Exp. etc			
To NET PROFIT (**) transferred to Capital A/c		(Note: (Either Net profit or Net Loss)	

Financial Statements: Balance Sheet

Statement of the financial position of a business as of a certain date.

Assets: Resources owned by a corporation, e.g., cash, accounts, receivable, equipment, land

Liabilities: Amounts / services owed by the company, e.g., loans payable, accounts payable, customer advances, etc.

Stockholders' equity:

- Initial investment by the owners (capital stock –common and preferred stocks)
- Plus the cumulative sum of undistributed profits (retained earnings)

Format of a Firm's Balance Sheet – Usual Items

Balance Sheet of (name of enterprise) as at (dd/mm/yy)

<u>Liabilities</u>		<u>Amount</u>	<u>Assets</u>		<u>Amount</u>
Sundry or Trade Creditors		....	Cash -in-hand including Petty Cash		....
Bills Payable		....	Cash at Bank		....
Bank overdraft		....	Bills receivable		....
.....					
Employees' Provident Fund		....	Sundry debtors/ Book debts		....
Loans (Cr.)		....	Loans (Dr.)		....
Mortgage		....	Closing stock		....
Reserve or Reserve Fund		....	Loose tools		....
Capital		....	Investments		....
<u>Add</u>	Interest on Capital	....	Furniture & fixtures		....
	Net Profit from P/L A/c	..... ..	Plant & machinery		....
			Land & Building		....
<u>Less</u>	Drawings	....	Patent & Trademarks		....
	Income tax	....	Goodwill		....
	Interest on drawings	....		
	Net loss	..... ..		
		=====			=====

Digital bookkeeping and accounting systems

- Excel spreadsheet
- Microsoft small accounting
- Quick book
- Peach tree, etc.



Practice Activity

- Uses the journal provided or any other bookkeeping system to register all your transactions for the last 3 years if not yet done

Or

- work on one the following case studys

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Case Studies: Comprehensive Exercises for Preparing Final Accounts and Solutions

CASE STUDY 1

Case Study 1: Exercise & Solution

From the Balance Sheet given below, calculate (i) *Fixed Assets*; (ii) *Current Assets*; (iii) *Current Liabilities*; (iv) *Capital employed*; and (v) *Working capital*

Liabilities	Amount	Assets	Amount
Trade Creditors	210,000	Freehold Premises	200,000
Outstanding expenses	16,000	Plant & machinery	160,000
Bank overdraft	24,000	Furniture & fittings	40,000
Long-term loan	100,000	Stock	240,000
Interest accrued on term loan	5,000	Trade debtors	180,000
Capital	467,000	Prepaid insurance	2,000
	<u>822,000</u>		<u>822,000</u>
	=====		=====
<u>(Note:</u>		<u>Solutions on the next</u>	
		<u>slide</u>	

Case Study 1: Solutions

(i) Fixed Assets Calculation		(ii) Current Assets Calculation	
Items	Amount	Items	Amount
Freehold Premises	200,000	Stock	240,000
Plant and Machinery	160,000	Trade Debtors	180,000
Furniture fittings	40,000	Prepaid insurance	2,000
	400,000		422,000
(iii) Current Liabilities Calculation		(iv) Capital Employed Calculation	
Trade Creditors	210,000	Method 1	
Outstanding Expenses	16,000	Capital	467,000
Bank Overdraft	24,000	Long term loan	100,000
Interest on Term Loan	5,000		567,000
	255,000	Method 2	
(v) Working Capital Calculation		Fixed Assets	400,000
Current assets as in item (ii)	422,000	Add Working capital	167,000
Current liabilities as in (iii)	(255,000)		567,000
	167,000		

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Case Studies: Comprehensive Exercises for Preparing Final Accounts and Solutions

CASE STUDY 2

Case Study 2: **Exercise**

From the following Trail Balance of Roger & Co. (an SME firm) prepare a (i) Trading Account; (ii) Profit & Loss A/c for the year ending 31 March 2009; & (iii) a Balance Sheet as on that date

Dr.	Amount	Cr.	Amount
Sundry debtors	1,500	Capital	25,000
Stock on 1 April 2008	5,000	Interest	600
Land and building	10,000	Sundry Creditors	7,000
Cash in hand	1,600	Sales	17,000
Cash at bank	4,000	Bills payable	4,000
Wages	3,000		
Bills receivable	2,000		
Interest	200		
Bad debts	500		
Repairs	300		
Furniture and fixtures	1,500		
Depreciation	1,000		
Rent and taxes	800		
Salaries	2,000		
Drawings	2,000		
Purchases	10,000		
Office expenses	2,500	Note: On 31 March 2009 the stock was valued at 10,000.	
Plant and machinery	5,700		
	53,600		53,600

Solution Case 2: Trading and Profit & Loss account of RG & Co. for 31 march 2009

Dr.		Cr.	
Particulars	Amount	Particulars	Amount
Opening balance	5,000	Sales	17,000
Purchase	10,000	Closing Stock	10,000
Wages	3,000		
To Gross Profit transferred to P/L A/c	9,000		
	27,000		27,000
Interest	200	Gross Profit transferred from Trading A/c	9,000
Bad debts	500	Interest	600
Repairs	300		
Depreciation	1,000		
Rent, rates and taxes	800		
Salaries	2,000		
Office Expenses	2,500		
Net profit transferred to Capital A/c	2,300		
	9,600		9,600

Solution Case 2: Balance Sheet of RG & co. as at 31 March 2009

LIABILITIES	AMOUNT	ASSETS	AMOUNT
<u>Current Liabilities</u>		<u>Current Assets</u>	
Sundry Creditors	7,000	Cash in hand	1,600
Bills Payable	4,000	Cash at Bank	4,000
	11,000	Bills receivables	2,000
<u>Capital</u>		Sundry debtors	1,500
Opening balance	25,000	Closing stock	10,000
<i>Less</i> Drawings	(2,000)		19,100
	23,000	<u>Fixed assets</u>	
<i>Add</i> Net Profit	2,300	Furniture and fixtures	1,500
	25,300	Plant and machinery	5,700
	36,300	Land and building	10,000
			17,200
	36,300		36,300



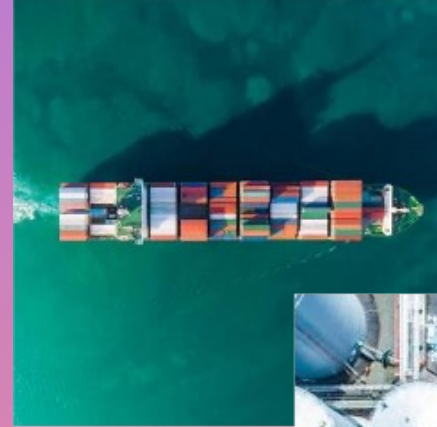
THANK YOU

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APPENDICES

CASE STUDY: Write a Cash Book

Dr.		<u>CASH ACCOUNT</u>		Cr.	
Increases	Amount	Decreases	Amount		
Opening balance	10,000	Payment for Purchases	5,600		
Cash Sales of Goods	5,000	Payment to Creditors	2,000		
Receipts from Debtors	7,000	Wages and Salaries	1,600		
Receipts from Commission	2,000 3,000	Rent	1,000		
Sales of fixed assets	500	Postage	200		
Rent received		Cartage	<u>100</u>		
			10,500		
		Closing balance	<u>17,000</u>		
	----- 27,500 =====		----- 27,500 =====		
	NOTE: Receiving Account is Debited		Note: Giving Account is Credited		

Trade Discount & Cash Discount

Trade Discount

Trade discount is allowed by one business enterprise to another, which is making a bulk / large purchase for resale to an ultimate customer.

Trade discount is allowed by the seller as a deduction in the invoice, and hence NOT recorded in the books of accounts. Only net amount is recorded.

Cash Discount

Cash discount is an allowance or deduction allowed to encourage prompt payment. Seller allows cash discount say @ 2% of invoice value to the buyer

The amount of cash discount is calculated after deducting trade discount from the invoice price. Cash discount is calculated always on net amount

Exercise on Trade & Cash Discounts

Question: On 28.02.09, Mr. XX sells goods to Mr. YY (giving trade discount of 2%) for a net amount of 80,000 allowing a cash discount of 5% for prompt payment within 15 days. Mr. YY pays on 10.03.09 within 15 days and gives a cheque to Mr. XX. Mr. YY pays 80,000 less 4000 (5% cash discount) = 76,000. Pass necessary entries in the books of Mr. XX

Solution:

In the Books of Mr. XX

Date	Particulars	Amt.	Date	Particulars	Amt
2009 Feb. 28	To Sales A/C	80,000	2009 March 10	By Bank A/C	76,000
			March 10	By Discount allowed A/C	4,000
		----- 80,000 =====			----- 80,000 =====
Dr.	Particulars	<u>Discount</u>	<u>Allowed</u>	Particulars	Cr.
Date		<u>Amount</u>	<u>A/C</u> <u>Date</u>		<u>Amount</u>
2009 March 10	To Mr. YY A/C	4,000			

Bank Reconciliation Statement

Meaning of Bank Reconciliation:

- ❑ Money *deposited* into a bank is recorded on the **Debit Side (Dr)** of a two-column Cash Book maintained by the enterprise, while all *withdrawals* are recorded on the **Credit Side (Cr.)**
- ❑ The Bank in its account of the enterprise, records all *deposits* made by the enterprise on the **Credit** Side (Cr.) and *withdrawals* on the **Debit** Side (Dr.) A copy of this account is given to the enterprise known as Pass-book or Bank Statement (hard or soft).
- ❑ As on a particular date, the balances appearing in the Cash Book of the enterprise and those in the Bank Account (or Pass Book or Bank Statement) should agree, but some times they do not .If the two differ, it becomes necessary to know the reasons /locate the missing entries. The statement to record the details to tally the balances is known as Bank Reconciliation Statement.

Bank Reconciliation Statement (contd.)

Definition: A Bank Reconciliation Statement is prepared on a particular date to reconcile the bank balance in the Cash Book with the balance as per the Bank Pass Book (Bank Statement) by showing the reasons / details for differences between the two.

This is an important process / statement to determine the exact cash position on a date for preparation of correct P/L account and Balance Sheet.

ILLUSTRATION & EXERCISE:

Prepare Bank Reconciliation Statement from the following data on 30.6.09:

Bank Statement showed a favorable (Cr) balance of 9,214 and Cash Book minus balance (Dr) of 5,914. Reconcile the balances of the two.

- (i) On 29.06.09 the bank credited the sum 1,650 in error.
- (ii) Certain cheques valued at 4,500 issued before 26.06.09 were not cleared.
- (iii) A hire purchase payment of 950 made by standing order was not entered in the Cash Book.
- (iv) A cheque for a sum of 600 deposited and credited by Bank was accounted as receipt in cash column of the Cash Book; and
- (v) Other cheques for 8,500 were deposited in June but cheques for 6,000 only were cleared and credited by the bank.

(See next slide for Solution)

Bank Reconciliation Statement (contd.) : SOLUTION

Bank Reconciliation Statement as on June 30, 2009

Particulars	Plus items (Amt)	Minus items (Amt)
Balance as per Pass Book (Cr.)	9,214	1,650
Less: Bank Credited in error		4,500
Cheques issued but not cleared	950	
Add: Hire purchase payment of 950 not entered in Cash Book		600
Less: Cheque deposited into Bank was accounted in Cash column in the Cash Book	2,500	
Add: Cheques deposited for 8,500 but cleared for 6000 (8500-6000)		5,914
Balance as per Cash Book (Dr.)	----- 12,664 =====	----- 12, 664 =====

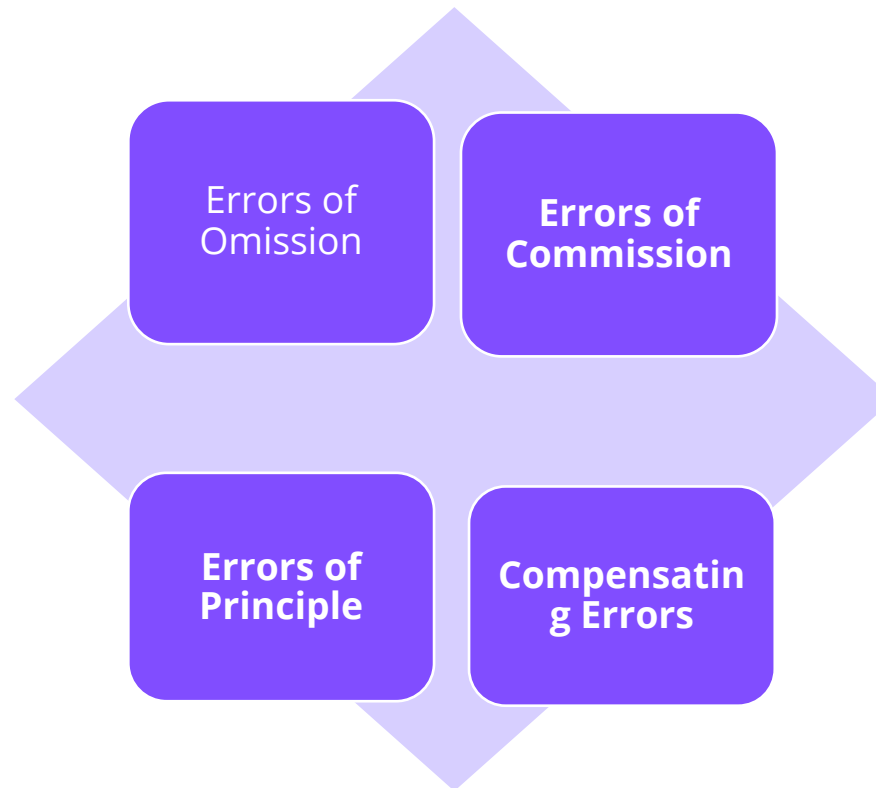
Common Practices

- Recording of monthly sales;
- Recording of income and expenses;
- Recording of inventory;
- Routine financial reporting;
- Budgeting financial reporting;
- Budgeting planning;
- Debt and Account Receivables recording;
- Bank account recording.

Rectification of Errors

Both sides (Dr. & Cr.) of the Trail Balance must agree. If they do not, efforts should be made to locate the errors and rectify. *The procedure followed to rectify the errors committed and to set right accounting record is called Rectification of Errors.*

Classification of Errors



Inventory

Three main concerns:

1. The physical goods to be included in the inventory?
2. The costs to be included in inventory?
3. The cost flow assumption to be adopted?



Physical goods to be included in inventory: Technically, purchases should be recorded when legal title to the goods passes to the buyer.

Cost of inventory includes costs of expenditures necessary (directly or indirectly) to bring an item to a salable condition and location.

Inventory

Two inventory systems:

1. Periodic Inventory System;
2. Perpetual Inventory System.



Inventory

The cost flow assumption:

- ❑ The actual physical flow of goods and the cost flow assumption are often quite different.
- ❑ There is no requirement that the cost flow assumption adopted be consistent with the physical movement of goods.
- ❑ 4 types of assumptions:
 - FIFO;
 - LIFO;
 - Average;
 - Specific Identification.

Depreciation

Depreciation is the process of allocating the cost of an asset to expense in the accounting periods benefiting from its use.

The importance of depreciation:

- All equipment at a certain time will have to be replaced;
- The older the equipment the less value the divestment price;
- The older the equipment the higher its maintenance costs;
- The older the equipment the more often break downs are experienced.



Depreciation

Value of Depreciation:

- Anticipating earlier mentioned problems, all equipment must have a depreciation value
- Depreciation value is in the form of back up fund in case the equipment needs replacing

$$\text{Depreciation Value} = \frac{\text{Equipment Investment Value}}{\text{Expected Equipment Lifetime}}$$

There are basically 2 methods of depreciation:

- Straight line depreciation;
- Accelerated depreciation.

Depreciation- Two Methods

Straight Line Method

An equal amount of depreciation is charged every year during the economic life of the asset to reduce the cost of asset to its residual value at the end of its economic life.

$$\text{Straight Line Method} = \frac{\text{Cost} - \text{less-Scrap Value}}{\text{Useful life}}$$

EXERCISE: Apply depreciation

$$\frac{1,20,000 - 20,000}{10 \text{ yrs.}} = 10,000$$

2006-07-	120,000 (asset cost)
less dep.	<u>10,000</u>
2007-08	110,000
less dep.	<u>10,000</u>
2008-09	100,000

Written Down Value Method

Under this method, depreciation is charged at a fixed rate on the reducing balance (i.e. cost-less-depreciation) every year.

EXERCISE: Suppose, the value of the asset is 20,000 and the percentage to be written off each year is 10. Apply depreciation

2006-07	20,000 (asset cost)
less dep. 10%	<u>2,000</u>
2007-08	18,000
Less dep. 10%	<u>1,800</u>
2008-09	16,200
less dep. 10%	<u>1,620</u>
	14,580