BUSINESS SENSE 101:

BASIC BOOK-KEEPING SKILLS

In partnership with

TUI CARE FOUNDATION

the Travel Foundation

Tourism Product Development Co. Ltd
TPDCo

INTRODUCTION

This is the second in a series of manuals, designed to help small and medium tourism businesses in Jamaica get to grips with some of the essential elements of business planning and management.

This manual aims to help you:

- Learn key accounting and book-keeping terms
- Understand the importance of keeping good records for your business
- Access practical tips to help you with your business book-keeping tasks

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https://www.pcsjm.com

WHAT IS ACCOUNTING? WHAT IS BOOK-KEEPING?

Accounting is the identification, accumulation, measurement & communication of economic data about an enterprise for decision makers & other interested parties.

Book-keeping is the activity or occupation of keeping records of the financial affairs of a business (Oxford Dictionary).

- Book-keeping is a foundation/base of accounting. Accounting uses information provided by bookkeeping to prepare financial reports and statements. Bookkeeping is one segment of the whole accounting system.
- Proper book-keeping ensures that you are always on top of your business, so that you are able to make wise financial decisions for the growth of your business/company.

Why is it important to keep good records?

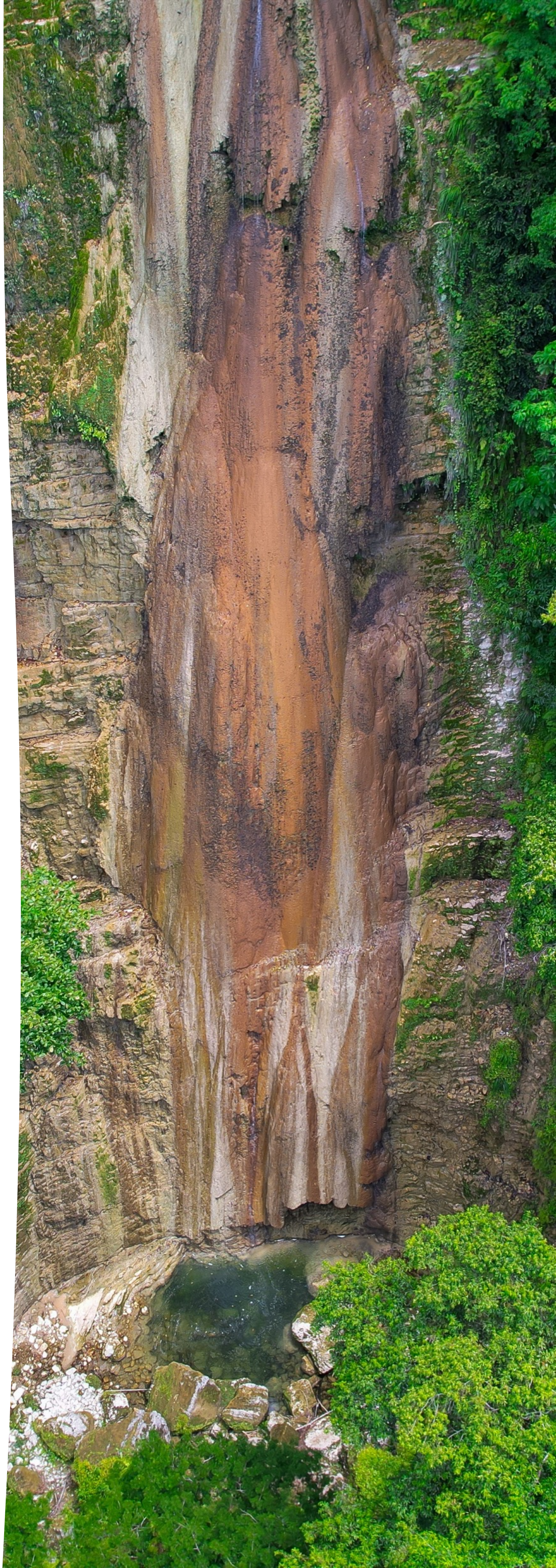
- For tax purposes, to:
  - Shorten the length of time to do a tax audit
  - Easily identify tax savings
  - Verify business expenses for tax audit purposes
  - Provide an accurate picture of your business operations
  - Easily obtain information about the financial position of a business

- For other purposes, to:
  - Make it quicker to prepare year end accounts
  - Help identify the strengths and weaknesses in your business
  - Make it easier to get a loan or sell your business

KEY ACCOUNTING TERMS

GENERAL TERMS

- **Accounting Period:** this defines the length of time covered by a financial statement or operation
- **Allocation**: this describes the procedure of assigning funds to various accounts or periods. For example, a cost can be allocated over multiple months or over multiple departments
- **Cash Flow**: the term used to describe the inflow or outflow of cash in a business
- **Business (or Legal Entity):** this is the legal structure, or type, of a business. Common company formations include Sole Proprietor, Partnership, and Limited Liability Corp. Each entity has a unique set of requirements, laws and tax implications
- **Debits and credits**: generally, when a transaction involves cash coming into the business, this is a debit. Conversely, when money leaves the business, the system will credit the cash account. To put it simply, debits are positive numbers, while credits are negative numbers.



BALANCE SHEET TERMS

The Balance Sheet gives you a snapshot of a company's financial strength at a specific point in time. The formula is:

Assets = Liabilities + Equity

- **ASSETS** are what you **OWN** (cash, accounts receivable, inventory/stock, fixed assets such as buildings:
    - **Accounts receivable** (sometimes called debtors or trade receivables)- is the account that records all outstanding client payments – i.e. the money owed to a business. If you sell services or provide products without collecting payment immediately, you will need to keep track of all the clients that owe you money.
    - **Inventory** - is the items that you sell to make a profit. You should ensure that the numbers accurately reflect the actual stock you hold by performing regular stock count. Therefore, the accounting system must be updated with the correct inventory cost and selling prices.
- **LIABILITIES** are what you **OWE** to any other person or organisation (accounts payable, short-term debt/bank loans/GCT payable or income tax payable)
    - **Accounts payable** (also referred to as creditors or trade payables) - this keeps track of accounts that your business owes to others. Examples include bank loans, unpaid bills and invoices.
- **EQUITY** is how much the company is worth on paper which includes money out into the business, money taken out of the business & earnings retained in the company. In other words, it is **the amount of money that would remain if a business sold all its assets and paid off all its debts.**

INCOME STATEMENT TERMS

This statement tells you whether or not you have made a profit over a given period of time.

The formula is

Revenue

-

Expenses

=

Profit

- **REVENUE** refers to income/sales aka what you earn from selling your products and/or services
- **EXPENSES** refers to what you spend. It can be broken down into Cost of Goods Sold and Overhead Expenses:
    - Cost of Goods Sold is the cost directly related to revenue aka what you spend to make what you earn (for example food and beverage costs, staff wages, licenses etc).
    - Overhead expenses refers to the cost to run the business, but are not directly related to revenue. This includes cleaning materials, marketing costs, training, accounting fees, legal fees, etc.

STATEMENT OF CASH FLOW TERMS

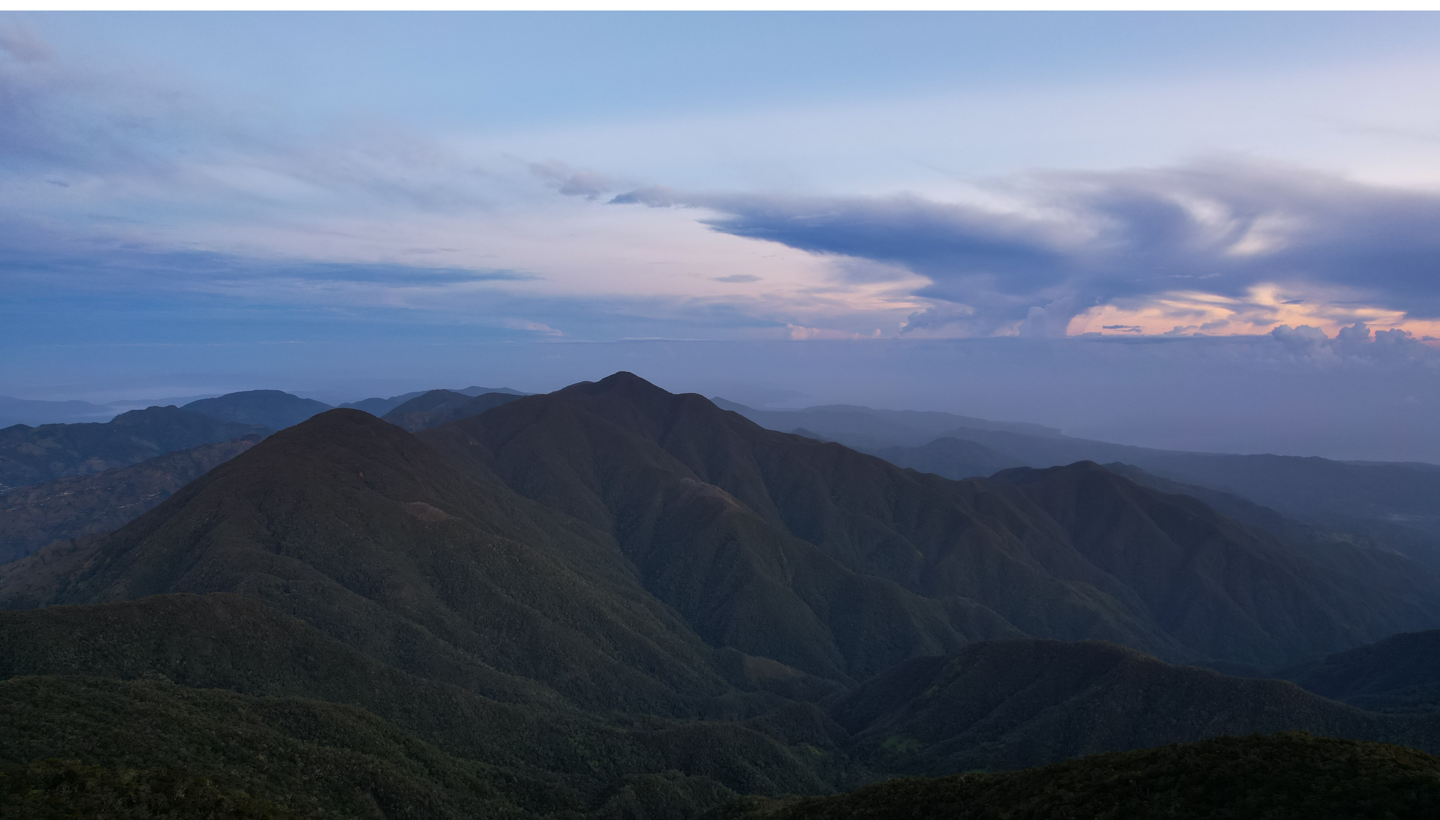
- **Operating Activities**: refers to cash collected from sales versus cash paid related to sales
- **Investing Activities**: captures new equipment purchased or sold
- **Financing Activities:** change in debt or inflow of capital

Phantom Books
Statement of Cash Flows
for the Year Ended December 31, 2012

Cash flows from operating activities[a]			
Net income	$ 51,000		Step 1
Adjustments (to convert net income to cash provided by operating activities)			
Add back depreciation expense	29,000		
Deduct gain on sale of equipment	(4,000)		
Add back loss on sale of long-term investment	8,000		
Decrease in accounts receivable	6,000		
Increase in merchandise inventory	(13,000)		
Decrease in prepaid expenses	4,000		
Decrease in accounts payable	(1,000)		
Increase in income tax payable	2,000		
Cash provided by operating activities		$ 82,000	
Cash flows from investing activities[b]			
Purchase of equipment	(27,000)		Step 2
Proceeds from sale of equipment	12,000		
Purchase of long-term investments	(25,000)		
Proceeds from sale of long-term investments	3,000		
Cash used by investing activities		(37,000)	
Cash flows from financing activities[c]			
Proceeds from note payable	5,000		Step 3
Repurchase of common stock	(16,000)		
Payment of cash dividends	(13,000)		
Cash used by financing activities		(24,000)	
Net increase in cash		$ 21,000	Step 4
Cash at beginning of year (from balance sheet)		24,000	
Cash at end of year (from balance sheet)		$ 45,000	

Basic book-keeping tasks include the following:

- Invoicing clients/customers
- Recording supplier invoices
- Recording vendor payments
- Recording client payments
- Updating your payroll system, where applicable
- Drawing financial reports



Basic book-keeping / accounting summarised

- Income Statement (Are you profitable?)
- Balance Sheet (Are you healthy?)
- Statement of Cash Flows (Where is cash going?)

Key Small Business Book-keeping Tips

1. Save and organize all your records and receipts (source documents). This includes payment receipts, invoices, payroll records, bank and credit card statements, Investment statements, tax returns, etc.

2. Determine which bookkeeping method (single-entry or double-entry; cash or accrual etc.) works best for you:

   a) Single entry bookkeeping - This is a straightforward method where one entry is made for each transaction in the books. These transactions are usually maintained in a cash book to track incoming revenue and outgoing expenses.

   b) Double entry bookkeeping - This is more robust. It follows the principle that every transaction affects at least two accounts, and they are recorded as debits and credits. In this system, the total credits must always equal the total debits. When this happens, your books are "balanced".

   c) Cash basis versus accrual - Transactions are usually recorded using the accrual method of accounting which requires that revenue is recorded when it is earned. Similarly, expenses are recorded when they are incurred, usually along with corresponding revenues. This is the opposite for cash basis. Transactions are recorded when money actually changes hands. This method is easier but can be misleading. The general practice used is the accrual basis.

   d) Manual bookkeeping (using Microsoft Excel or paper journals) or online cloud based accounting software like Quickbooks, Xero, Wave app, etc.

3. Regularly record your source documents in your accounting system: daily or weekly.

4. Keep tabs on your cash flow. To effectively run your business, you should keep a close eye on money coming in (expected to come in) and going out of the business. Ensure to follow up with clients for payments and likewise ensure to pay your bills in a timely manner.

5. Prepare financial statements (Balance Sheet, Income Statement and Cash Flow Statement). These statements answer the following questions - are you profitable? Are you healthy? Where is cash going?

6. Work towards tax compliance. Ensure to file and pay your taxes at the required deadline to avoid spending more than you should.

7. Seek help when in doubt. Reach out to an accounting/tax professional to assist you to effectively manage your financial and taxation needs. They are the experts...let them do the job while you focus on managing your business.

Characteristics of a good accounting system

Reliable

- The information itself needs to be error free. If you're second guessing your accounting system, there's a major problem. Before you blame the system make sure everything was set up correctly as the system can only work with the information it is fed.

Relevant

- Information is relevant if it influences business decisions. For an accounting system to provide relevant information the information must be available on time and have a level of detail significant enough to show trends, comparisons and other information that fuels business decisions

Easy to understand

- The more guesswork involved in an accounting system, the more prone a company is to error. If the accounting system in user friendly and easy to understand, the more chance the accounting system has of being implemented to its full capacity

Comparable

- A great accounting system has easy to access reports that are comparable across business units and periods to identify trends. To be comparable, accounting reports must belong to a period, use common unit of measurement and a common format of reporting

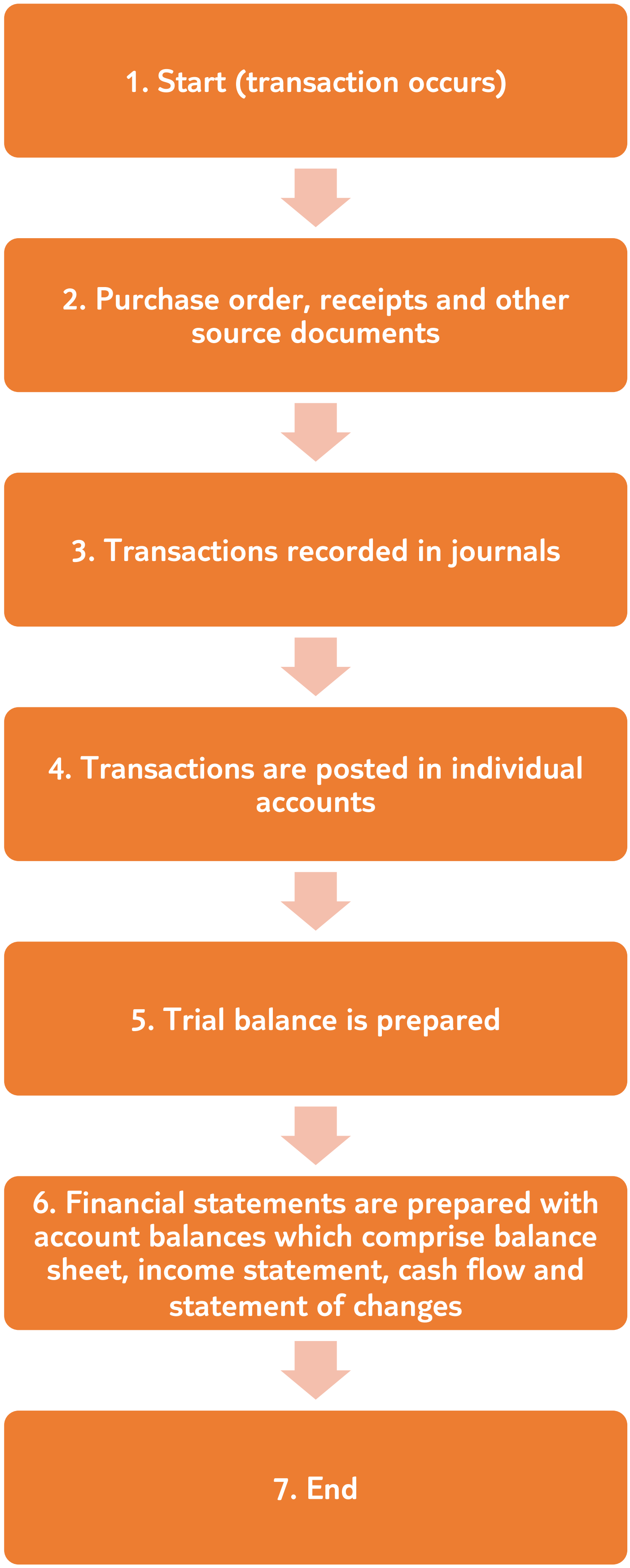
Accessible

- When running your business, it is essential that you're able to quickly and efficiently access date to troubleshoot and map out future plans for not only efficiency but also success

Useable

- Employees and managers need to be able to use thee accounting system with minimal effort and a small learning curve. An otherwise good system that is counter-intuitive to your accounting needs can hinder productivity.

Flow of transactions through the accounting system



Annex – extra information to consider

Guide to creating an expense report:
https://quickbooks.intuit.com/global/resources/expenses/expense-report-template/

Three templates have been provided to accompany this manual, available to download from the Resources section of the Big Up Small Business website: www.bigupsmallbusiness.org

1. Expense report template
2. Expense schedule template
3. Purchase ledger template

Recording transactions

Recording transactions begins with the source documents like purchases and sales orders, bills, invoices and cash register tapes. Once you gather these documents, you can record the transactions using journals, ledgers & trial balance.

- **Journals** - the journal is called a book of original entry. It is a place where businesses chronologically records its transactions for the first time. It can either be physical or digital.
- **The ledger** is a book or a compilation of accounts. After entering transactions in a journal, they are classified into separate accounts and then transferred into the ledger.
- **Trial balance** is produced from the compiled and summarized ledger entries. The trial balance is like a test to see if your books are balanced. It lists the accounts exactly in the following order: assets, liabilities, equity, income and expenses with the ending account balance.

For example:

Date	Account Name	Debit ($)	Credit ($)
2-Aug	Office Supplies	$ 4,000.00	
	Cash		$ 4,000.00
Purchase of office supplies worth $4,000			
5-Aug	Purchase	$ 7,000.00	
	Cash		$ 2,000.00
	Accounts Payable		$ 5,000.00
Purchase of goods from Screens R Us worth $7,000 paid for with $2,000 in cash and $5,000 in credit.			
12-Aug	Cash	$ 10,000.00	
	Accounts Receivable	$ 5,000.00	
	Sales		$ 15,000.00
Sales of goods to Macro Computing worth $15,000 paid for with $10,000 in cash and $5,000 on credit			
20-Aug	Bank Loan Payable	$ 3,000.00	
	Cash		$ 3,000.00
Payment for bank loan worth $3,000.			
25-Aug	Accounts Payable	$ 1,000.00	
	Cash		$ 1,000.00
Payment of $1,000 to Screens R Us for earlier purchase made on credit			
28-Aug	Cash	$ 5,000.00	
	Acounts Receivable		$ 5,000.00
Payment of $5,000 received from Macro Computing for earlier sales made on credit			
30-Aug	Payroll Expense	$ 2,000.00	
	Payroll Tax	$ 300.00	
	Cash		$ 2,300.00
Paid employees $2,300 in wages			

How do the journal entries match to the trial balance?

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Adjusted Trial Balance
January 31, 2019

Account	Debit	Credit
Cash	$24,800	
Accounts Receivable	1,200	
Interest Receivable	140	
Supplies	400	
Equipment	3,500	
Accumulated Depreciation: Equipment		$ 75
Accounts Payable		500
Salaries Payable		1,500
Unearned Revenue		3,400
Common Stock		20,000
Dividends	100	
Interest Revenue		140
Service Revenue		10,100
Supplies Expense	100	
Depreciation Expense: Equipment	75	
Salaries Expense	5,100	
Utility Expense	300	
Total	$35,715	$35,715

Interest Receivable

Jan. 31	140		
	Bal. 140		

Supplies

Jan. 30	500	100	Jan. 31
	Bal. 400		

Accumulated Depreciation: Equipment

		75	Jan. 31
		Bal. 75	

Salaries Payable

		1,500	Jan. 31
		Bal. 1,500	

Unearned Revenue

		4,000	Jan. 9
Jan. 31	600		
		Bal. 3,400	

Service Revenue

		5,500	Jan. 10
		2,800	Jan. 17
		1,200	Jan. 27
		600	Jan. 31
		Bal. 10,100	

Interest Revenue

		140	Jan. 31
		Bal. 140	

Supplies Expense

Jan. 31	100		
	Bal. 100		

Salaries Expense

Jan. 20	3,600		
Jan. 31	1,500		
	Bal. 5,100		

Depreciation Expense: Equipment

Jan. 31	75		
	Bal. 75		

Key accounting concepts

MATCHING: The matching concept says that you should record revenue and expenses related to revenue at the same time. The purpose is to let you see any cause-and-effect relationship between income and purchases

- ***Rule: Record expenses related to revenue in the same period as the revenue***

ECONOMIC ENTITY : One of the most important concepts for small businesses - you should avoid comingling business with personal funds. Business financial statements should only reflect business transactions.

- ***Rule: Don't co-mingle personal and business finances***

GOING CONCERN: This concept says you should assume that your business is in good financial condition and will remain in operation for the foreseeable future. This concept allows companies to sometimes defer the recognition of certain expenses into future accounting period.

- ***Rule: Assume the business entity in in good standing and will continue***

DUALITY: In accounting, every transaction has an equal and corresponding effect. That is, it affects two accounts. Every financial transaction is recorded in two accounts as debits and credits. Because a debit in one account cancels out credit in another, all debits must equal all credits. This concepts forms the basis of double entry accounting:

- Debit: When a transaction is classified in this double entry system, debit refers to the increase in assets and expenses
- Credit: refers to decrease in assets and expenses

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