Accounting Concepts for Business and Individual Success

Introduction:

Accounting for what happens to you the individual or you the business owner is vital to your success. The amount of money being controlled is not important, because whether it is $10 or $100,000 it is all relative to the value it has in your life and your business. The secret is in knowing how to track those dollars to know how, when, where and how much is being received, and even more important, being spent. This article will explain the key concepts that will help you understand what information needs to be kept and the importance of good record keeping.

What is Accounting?

Most of us are familiar with the term “bookkeeping” which is the recording of the accounts and transactions of a business. “Accounting” is those bookkeeping methods used to make a financial record of business transactions to prepare statements of the assets, liabilities and operating results of a business. Just think of it as a way of tracking or keeping a record of:

1) How much money did I make or bring in? (Revenue)
2) How much money did I pay out? (Expenses)
3) How much money did I spend to make that money? (Cost of doing business)
4) How much money is left? (Profit or Loss)

Revenue

Revenue is income (inflows) from a particular source, whether from producing goods, providing services or other activities. Income can be received in the form of paychecks for the individual. For the business owner income is derived from sale receipts with payments by cash or credit card and/or check payments from invoicing customers.

Expenses

Expenses are amounts paid (outflows) for goods and services to attain a goal or accomplish a purpose. For example, paper and ink purchased to print the invoices for customers are office supplies expense. Generally, these are necessary expenses to get the job done.

Cost of doing business

We understand that there are expenses (defined above) that must be purchased in order to get the job done. However, there are other costs that may not be as obvious as "office supplies" that still need to be considered. They are not readily identified with a particular activity, but are necessary for the general operation of the business. They are indirectly related to the accomplishment of a purpose. For example, if you have a home office you will have expenses for office supplies and etc. But also a proportionate amount of utilities (electricity and gas) of the household is also a cost of doing business.

Profit or Loss

Profit (gain) is the sales of the business less costs such as wages, fuel, depreciation and other costs. It can be explained as the amount of income that remains after costs are deducted. This increases the equity (worth) of the business. Loss is the excess of expenses over income, or you have spent more than you made. It decreases the equity of the business. The profit and loss principles can be applied also to an individual's income and spending situations.

How to keep good records:

Business:

Good record keeping starts before you go into business by deciding how you will track your income and expenses. This decision should be included when you write your original business plan. If funds are available you can purchase accounting software such as QuickBooks, which is a great starter package for a beginning business that wants to manage its own bookkeeping. An alternative is to outsource the accounting of your business to a company that provides accounting services. (I recommend that as part of your start-up costs you allow enough money to have a professional set up your books to record your capital accounts and provide training if needed.) If you cannot afford to invest in an accounting package, at the very least utilize excel spreadsheets to record revenues and expenses.

Indivdual:

Just as a business tries to make a profit, so should an individual develop a budget and keep spending within their means. It is equally important for an individual to maintain receipts for expenses that may allow deductions at tax time. These can be tracked by reviewing and highlighting items on your monthly bank statement or even simply keeping receipts in a file box for year-end review. The secret is to be consistent and seek financial advice that will help you minimize your tax liability.

When Good Records Are Not Kept

The lack of good records has many consequences. These include:

1) Not knowing the financial state of your business at a point in time.
2) Inability to track cash for possible under or over payments.
3) Failure to record items that have a negative/positive tax impact.
4) Limits the ability to maximize benefits from legal tax structures.
5) Exposure to a tax audit by the IRS.

Summary:

This information is presented as general advice for successful record keeping to the aspiring business owner and individual concerned with management and control of their finances. Accounting is an extensive subject and there are additional topics of equal importance that have not been mentioned. These topics include but are not limited to the accounting conceptual framework, the basic elements including assets, liabilities and proprietorship, capital assets and depreciation, cash versus accrual accounting and others too numerous to mention. Their subject matter would require hours of study and would prove overwhelming at this time. However, the information presented should be sufficient to help the beginning business owner take steps in the right direction.

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