**Name** **Kashif Ahmed**

**Id** **14225**

**Subject** **Introduction to Financial Accounting**

**Program** **BBA**

**Submitted To** **Sir Naveed Azeem Khattak**

# Summers (Final Term)

**Q#1. As a business activity what you understand about partnership form of business. Explain in detail the advantages and disadvantages of partnership form of business.**

**ANS. Partnership:**

A business partnership is a legal relationship usually formed by a written agreement between two or more individuals or companies. Partners invest their money in the business and each partner benefits from any profits and retain some of the losses.

The partnership as a business often has to be registered in all the states in which it operates. Each state can have many types of partnerships that it can form, so it is important to know the possibilities before enrolling. There are three types of partnerships:

- **General partnership:**

  In a general partnership, each partner shares equally with the workload, responsibility and profits generated and paid to the partners. All partners participate actively in the activities of the company.

- **Limited partnership:**

  Limited partnerships allow third-party investors to buy a business, but maintain limited responsibility and commitment based on their contributions. It is a more complex form of partnership, which also has more flexibility in ownership and decision-making.

- **Joint venture:**

  Short-term projects or alliances that bring together multiple partners for a project are usually structured as consortia. If the business performs well, it can continue as a general partnership. Otherwise, it may be closed.

**Advantages of a business partnership:**

- Two heads (or more) are better than one.
- Your business is easy to fix and the startup cost is low.
- More funds are available for the business.
- More lending capacity is achieved.
- High-level employees can become partners.
- The possibility of allocating income, an advantage of particular importance due to the resulting tax savings.
- Partners' activities are private.
- There is a limited external definition.
- It is easy to change your legal structure later if situations change.

**Disadvantages of a partnership:**

- Partners' responsibility for the company's liabilities is unlimited.
- Each partner is "intersocial" responsible for the debt of the partnership, i.e. that each partner is responsible for its share of the partnership's debts, and for being responsible for all debts.
- There is a risk of disagreement and friction between the partners and the administration.
- Each partner is a representative of the partnership and is responsible for the actions of other partners.
- If partners join or leave, they will probably need to evaluate all of the partnership's assets and this could be costly.

**Q#2. Two popular methods of financial statement analysis are time series analysis and periodic analysis. Explain the difference between these two methods. What are the different tools that an analyst uses to adapt for the analysis? Explain the tools with proper formulas.**

**ANS.** Financial analysis is the process of evaluating companies, projects, budgets and other financing-related operations to determine their performance and suitability. Typically, financial analysis is used to analyze whether a unit is stable, solvent, liquid, or profitable enough to justify a monetary investment.

**Time Series analysis:-**

Time series analysis can be useful to see how a given asset, security, or economic variable changes over time. It can also be used to investigate how changes related to the selected data point compare with changes to other variables over the same time period.

**Periodic analysis:-**

When you use periodic analyses, you will be notified by the system of the exceptional situations specified in the exceptions. The existing dataset is systematically checked for exceptional situations at a frequency you select (hour, weekly, monthly). If an exceptional situation occurs, you or another recipient will be notified by mail or fax, or you can initiate a workflow transfer that will eventually trigger a trace processing process.

There are two types of periodic analyses:

- Event-driven
- System-driven

**Difference between Time series analysis and periodic analysis:-**

Time series analysis is a statistical technique that deals with time series data or trend analysis. Time series data means that the data is in a series of specific periods or intervals. The data are examined in three types:
**Time series data:** A set of observations on the values that a variable takes at diverse times.
**Cross-sectional data:** Data of one or more variables, together at the same point in time.
**Pooled data:** A combination of time series data and cross-sectional data.
This method predicts the value for the following period based on the previous and current value. This includes calculating the average of the data so that the non-systematic data in each case or observation are mutually lubricated. The exponential equalization method is used to predict the short-term prediction period. Alpha, Gamma, Phi, and Delta are parameters that estimate the effect of time series data. Alpha is used when seasonality is not in the data. Gamma is used when a row tends to data. Delta is used when seasonal cycles are in the data. A model is applied according to the data pattern.

**Tools of Financial System Analysis:-**

1. Comparative Statement or Comparative Financial and Operating Statements.
2. Common Size Statements.
3. Trend Ratios or Trend Analysis.
4. Average Analysis.
5. Statement of Changes in Working Capital.
6. Fund Flow Analysis.
7. Cash Flow Analysis.
8. Ratio Analysis.
9. Cost Volume Profit Analysis

- **Comparative statement:-**Comparative statements deal with the comparison of different items of the Profit and Loss Account and Balance Sheets of two or more periods. Separate comparative statements are prepared for Profit and Loss Account as Comparative Income Statement and for Balance Sheets.

- **Comparative Income Statement**:- Three important data are obtained from the Comparative income Statement. These are gross profits, operating results and net results. Changes or improvements in business profitability can be found over a period of time. If the changes or improvements are not satisfactory, management can find out the reasons and some corrective action may be taken.
- **Comparative Balance sheet**:- The financial situation of companies may be unknown through the preparation of the comparative balance sheet. The different balance sheet items are used over two different periods. Assets are classified as assets and assets for comparison. Liabilities are also classified as current liabilities, long-term liabilities and shareholders' net worth. The net value of shareholders includes equity, preferred funds, reserves and surpluses and the like.
- **Common size statement:-** Below is the vertical presentation of financial information to prepare declarations of common dimension. Furthermore, the rupee value of the contents of the financial statements is not taken into account. However, only the percentage is taken into account in the preparation of the joint statement on size.
- **Trend analysis:-** The relationship between different records for different periods is to discover and then be compared during this analysis. Analyzing key relationships over a period of years provides an idea of whether the business problem is trending up or down. This analysis is otherwise referred to as a pyramid method.
- **Average analysis:-** Each time trend rates are calculated for a business concern, these rates are compared to the industry average. These two trends can be presented on paper and in the form of curves. This presentation of events in the form of images makes the analysis and comparison more complete and impressive.
- **Fund flow analysis-** detailed sources and the implementation of risk capital for a specific period. It indicates where the funds come from and how they are used during the period taken into account. Highlights the changes in the company's financial structure.
- **Cash flow analysis-** based on the circulation of money and banking instruments. In other words, the movement of money instead of working capital will be examined in the cash flow situation. There are two types of cash flow. These are actual cash flows and theoretical cash flows.
- **Ratio analysis-** is an attempt to develop a meaningful relationship between individual items (or group of items) in the balance sheet or profit and loss account. The analysis of proportions is useful not only for internal parts related to companies, but also useful for external parties. The analysis of the indicators highlights liquidity, solvency, profitability and capital orientation.

**Q#3. Fun App Company has the following liability accounts after posting adjusting entries: Accounts Payable $77,000, Unearned Ticket Revenue $36,000, Warranty Liability $25,000, Interest Payable $10,000, Mortgage Payable $150,000, Notes Payable $100,000, and Sales Taxes Payable $14,000. Assume the company's operating cycle is less than 1 year, ticket revenue will be recognized within 1 year, warranty costs are expected to be incurred within 1 year, and the notes mature in 3 years.**

**Instructions (a) Prepare the current liabilities section of the balance sheet, assuming $40,000 of the mortgage is payable next year. (b) Comment on Fun App Company's liquidity, assuming total current assets are $350,000.**

**ANS. (a)**

| **Current liabilities** | |
|---|---|
| Account payable | $ 77000 |
| Unearned ticket revenue | $ 36000 |
| Warranty liabilities | $ 25000 |
| Interest payable | $ 10000 |
| Sales tax payable | $ 14000 |
| Mortgage payable | $ 40000 |
| **Total current liabilities** | **$ 202000** |

**b)** Using the current assets information we calculate the current ratio for fun app company.

Current ratio = Current assets /Current liabilities

Current ratio= 350,000/202,000=1.7327

From the above information it shows that Current Ratio Fun App Company is greater than one indicates the company has the financial resources to remain solvent in the short term. However, because the current ratio at any one time is just a snapshot. It is usually not a complete representation of a company's liquidity or solvency.

**Q#4. Explain the following term in detail:**

- **Matching principal.**
- **Costing principal**
- **Concept of going concern assumption.**
- **Monitory unit assumption.**
- **Economic entity assumption.**
- **Time period assumption**

**ANS. <u>Matching principle:</u>**

The matching principle is one of the main accounting guidelines on which they are based. The relevant authority instructs an entity to report an expense to its profit and loss account during the period in which the corresponding revenue is received. In addition, it results in an obligation to be included in the balance sheet for the end of the accounting period. The mail principle is linked to the specialization base for file files and customizations.

If expenditure is not directly linked to income, the expenditure is recognized in the income account for the year in which it expires or is consumed. If the future benefit of a cost cannot be determined, the cost must be charged immediately.

### Examples:

Expenditure shall relate to the period during which they were incurred and not to the period during which it was paid. For example, if a company pays a 20% commission to the sales representatives at the end of each month. If the company has $100,000 in sales in December, the company will pay a commission of $1,000 next January.

## Costing principle:

Cost principle is an accounting policy that records assets in their cash at the time of purchase or purchase of the asset. The amount of the subscribed asset cannot be increased for improvements in market value or inflation, nor can it be updated to reflect any depreciation. Registered assets may include assets, liabilities and possibly short- and long-term own funds, and these assets are always recorded at their initial cost.

Financial assets can often monitor depreciation or the increasing value of acquired assets, but the cost principle will remain the same. In addition, the cost policy is also called a historical cost principle, which means that regardless of the increase in value or depreciation that a fixed asset passes over time, the initial cost of the fixed asset at the acquisition date is the value that is maintained as a cost policy.

## Concept of going concern assumption:

The concept of going concern is the assumption that a unit will be operational for the foreseeable future. On the contrary, this means that the company will not be obliged to cease operations and liquidate its assets in the near future at very low fire prices. In this case, the auditor is entitled to defer the recognition of certain costs for a later period, when the entity is likely to continue to operate and use its assets as efficiently as possible.

An undertaking is considered to be an ongoing activity in the absence of significant information to the contrary. An example of this opposite information is the inability of an entity to fulfill its obligations, as it is due without significant asset sales or debt restructuring. If this is not the case, one entity would purchase significant assets for the purpose of terminating its business and reselling the assets to the other party.

## Monetary unit assumption:

The monetary unit assumption (also known as the concept of money measurement concept) shows that only these events and transactions are recorded in the accounts of companies that can be measured and expressed in monetary terms.

The monetary unit is a simple and universally recognized basis for the communication of economic information. It is the most appropriate and effective basis for recording, communicating and analyzing economic data on the basis of which rational business decisions can be taken.

A concept very closely related to the currency hypothesis is the assumption of the fixed value of the dollar, which means that the dollar (or any other currency) does not lose its purchasing power over time. The fact that money loses its purchasing power due to inflation is ignored when recording accounting transactions.

## Economic entity assumption:

The economic entity assumption is an accounting authority that separates transactions made by the owner's business. It may also relate to the separation between the different departments of a company. Each unit maintains its own accounting records specifically for business activities.

Many external stakeholders use the records maintained by a company. Governments and investors use a company's financial records to evaluate its performance. Therefore, it is important that the transactions accurately reflect the activities of the company.

According to the economic entity assumption, a person evaluating a company's records assumes that all business-related transactions are reviewed. The sole beneficiary must keep its business transactions separate from its personal transactions. The case also concerns companies with different types of activities.

**Example:**

If one company manages two business departments – one is a hotel chain and the other is a restaurant chain – a separate accounting must be kept for each department. The costs of one business cannot be combined with the other. Keeping separate records will help the company know the true value of each line of business.

## Time period assumption:

Time period assumption is the period during which an undertaking divides the ongoing business into shorter accounting periods to prepare the financial statements.  The time period is usually monthly, quarterly or annual. The life of a company will continue for a long time, but the auditor must prepare a report to show the company's performance and financial position for management to make a correct and timely decision. Annual reports are usually called the natural year, and each report is lower than the one called an interim report.

The synchronization assumption will be the title of the entity's financial statements, such as the outcome statement, balance sheet and cash flow. The earnings statement will show us the company's results in a month, quarterly or year period. On the other hand, the balance sheet will show the financial position of the accounting equation (Asset = Liability + Equity). Finally, the cash flow statement will show the change in the company's cash flow during an accounting period.