

# Module 1 – Introduction to Accounting

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# 1.0 Learning Outcomes

In this chapter your will learn the followings:

- a) Understand accounting process.
- b) Understand the important of accounting.
- c) Explain and different various type of accounting.
- d) Understand Accounting in career path.
- e) Explain and recognize different type of entities.

# 1.1 What is Accounting?

Accounting is the process of recording financial transactions pertaining to a business.

The accounting process includes summarizing, analyzing and reporting these transactions and convert into a readable report for business owner to evaluate and understand their business performance.

Proper accounting allows a company's management to better understand the financials of its business.

This is so they can strategically plan its future expenditures in order to maximize profit.

## 1.2 Importance of Accounts

### 1.2.1 To understand your business well

To run a business you need data, records, reports, analysis, accurate information about assets, debts, liabilities, profits; and that is why Accounting is Importance for any business activities.

### 1.2.2 To make decision

Should you buy that brand new, top-of-the-line printer for the office? Well, that depends on whether you can afford it.

OK, how about your expenses? Is there anything you need to cut to help your business's bottom line? That depends on how much you're spending and on what.

To answer questions like these, you need to look at data—your accounting records, to be exact.

Accounting can help guide the decisions you make so you avoid common business mistakes, like overspending.

### 1.2.3 Compliance Purpose

Business owner duty and responsibility to declare and submit business report to:

- Inland Revenue Board
- The Companies Commission of Malaysia
- Bursa Malaysia

### 1.2.4 Financing Purpose

Investors and lenders need to learn a little bit about you before they invest or lend you money. And that means they analyzing into your business's accounting books.

Generally, you must show investors and lenders your business's financial statements. That way, they can obtain information about your profitability.

Your profit unable to justify if you are unable to provide a valid and reliability accounting record.

## 1.3 Types of Accounting

As a result of economic, industrial, and technological developments, different specialized fields in accounting have emerged.

The famous branches or types of accounting include:

- a) Financial Accounting
- b) Management Accounting
- c) Cost Accounting
- d) Taxation
- e) Auditing

### 1.3.1 Financial Accounting

Financial accounting involves recording and classifying business transactions and preparing and presenting financial statements to be used by external users.

In the preparation of financial statements, strict compliance with generally accepted accounting principles or MFRS is observed. Financial accounting is primarily concerned in processing historical data.

### 1.3.2 Management Accounting

Managerial or management accounting focuses on providing information for use by internal users, the management.

This branch deals with the needs of the management rather than strict compliance with generally accepted accounting principles.

Managerial accounting involves financial analysis, budgeting and forecasting, cost analysis, evaluation of business decisions, and similar areas.

### 1.3.3 Cost Accounting

Often considered as a subset of management accounting, cost accounting refers to the recording, presentation, and analysis of manufacturing costs.

Cost accounting is very useful in manufacturing businesses since they have the most complicated costing process.

Cost accountants also analyze actual costs versus budgets or standards to help determine future courses of action regarding the company's cost management.

### 1.3.4 Tax Accounting

Tax accounting helps clients follow rules set by tax authorities.

It includes tax planning and preparation of tax returns. It also involves determination of income tax and other taxes, tax advisory services such as ways to minimize taxes legally, evaluation of the consequences of tax decisions, and other tax-related matters.

## 1.4 Accounting Career Path



## 1.5 Types of Entities

### 1.5.1 Sole Proprietorship

This is a business run by one individual for his or her own benefit.

It is the simplest form of business organization. Proprietorships have no existence apart from the owners.

The liabilities associated with the business are the personal liabilities of the owner, and the business terminates upon the proprietor's death.

The proprietor undertakes the risks of the business to the extent of his/her assets, whether used in the business or personally owned.

Single proprietors include professional people, service providers, and retailers who are "in business for themselves."

Although a sole proprietorship is not a separate legal entity from its owner, it is a separate entity for accounting purposes. Financial activities of the business (e.g., receipt of fees) are maintained separately from the person's personal financial activities (e.g., house payment).

### **Sole Proprietor Taxation**

The individual and the business are considered to be the same entity for tax purposes.

### **The advantages of a sole proprietorship are:**

- Simple to organize
- Simple tax filings
- No double taxation
- Complete control by the owner

### **The disadvantages of a sole proprietorship are as follows:**

- Unlimited liability
- Self-employment taxes must be paid by the owner
- The only provider of equity to the business is the sole owner



## 1.5.2 Partnership

A partnership business entity, or a general partnership, is a business consisting of two or more owners who run their business in accordance with the terms of an oral or written partnership agreement.

Although an agreement is not required, it makes sense to have one so that the partnership will run smoothly.

### **Characteristics of a Partnership**

Simply co-owning rental property or sharing expenses does not constitute a partnership for tax and legal purposes.

To determine whether a partnership exists, authorities consider:

- Whether a partnership agreement exists and if the partners have adhered to its terms.
- The parties' relationships with one another.
- What each person contributes to the partnership.
- The level of control each person has over the income of the partnership and how it is used.

Every partner may enter contracts on behalf of the business unless the partnership agreement states otherwise.

Partners are jointly responsible for all business debts, obligations, and liabilities. This means that personal assets can be seized to pay these obligations.

## **Advantages of a Partnership**

With a general partnership, you can take advantage of a lean business model and make fast decisions on behalf of growth.

This type of entity is usually inexpensive to create, though you may want to hire an attorney to draft a general partnership agreement.

## **Partnership Taxation**

Partnerships are taxed as pass-through entities, which means that each partner reports a share of business profits and losses on his or her individual tax return.

The business itself is not subject to income tax at the corporate level.

As with sole proprietorships, some business expenses can be deducted depending on the specifics of your personal return.

## **Disadvantages of a Partnership**

The main negative aspect of a partnership is the liability that partners must assume for business debts and obligations.

This means creditors can seize not only the business assets but also partners' personal assets.

### **1.5.3 Limited Liability Partnership**

A limited liability company (LLC) combines the features of corporations and partnerships, which makes them an ideal entity for many businesses.

### **Advantages are:**

- The liability of investors is limited to the amount of their investments in the LLP
- An LLP can be structured so that the income earned by the business flows directly through to investors
  - An LLP can be run by professional managers, rather than a general partner
  - There is no limitation on the number of investors in an LLP

### **The disadvantages of an LLP include:**

- There will be annual government fees charged to maintain an LLC entity

### **LLP Taxation**

- taxed as a separate entity

## 1.5.4 Sendirian Berhad / Private Limited Company

A Sdn Bhd company is a private company limited by shares and is the most common business entity in Malaysia.

It is a separate legal entity which is capable of earning incomes, owning properties, signing contracts, suing another entity, and getting sued on its own name, separating your liabilities from the company itself. Since the updates of the Companies Act 2016 came into effect, you can register a Sdn Bhd as the only director and shareholder of the company without other business partners.

### **Advantages of a Sdn Bhd**

- It is relatively cheap to register.
- It has relatively simple compliance to follow as compare to listed company
- It separates your personal liabilities from the company itself.

- It is able to scale by increasing paid-up capital and issuing shares to investors.
- It can be 100% foreign-owned.

### **Disadvantages of a Sdn Bhd**

- It is unable to expand beyond 50 shareholders.
- It is unable to raise funds from the public.
- The transfer of shares is restricted.

## 1.5.5 Berhad / Public Limited Company

Similar to a Sdn Bhd company, a Bhd company is a company limited by shares with a few differences.

It can offer shares to the public without a limit on the number of shareholders, requires at least 2 directors and is governed by Bursa Malaysia Securities Berhad and the Security Commission of Malaysia.

The registration of this business entity can be time-consuming and expensive due to strict compliance requirements.

However, funding for the company would be easier to obtain since it is publicly listed on the market.

### **Advantages of a Bhd**

- It is easier to raise funds as the company is listed.
- It is able to raise funds from the public by issuing shares.
- It has flexible ownership of shares.

### **Disadvantages of a Bhd**

- It is costly and difficult to register.
- It has strict compliance to follow.