



Ethical Decision Making in Hospitality Businesses

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Table of Contents:

- Introduction of financial accounting
- Accounting Concepts
- Fundamental concept of accounting
- Liabilities
- Application and importance of accounting
- Financial accounting and its importance
- Key Principles of accounting
- Accrual accounting
- Revenue Recognition Principle
- Matching principle
- Introduction and key components of balance sheet, income statement and cash flow statement
- Relationship between the balance sheet, income statement, and cash flow statement.
- Examples of statements in real life and in numerics
- CONCLUSION

- Reference
- Appendix

Abstract:

The analysis highlights how the income statement measures profitability over a period, while the balance sheet presents the financial position of a company at a specific point in time. The cash flow statement complements these by explaining the inflow and outflow of cash from operating, investing, and financing activities. Together, these statements provide a comprehensive view of an organization's financial health and operational efficiency.

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The Basic Theoretical Concepts of Accounting

The fundamental concepts of accounting, including the accounting equation (Assets = Liabilities + Owner's Equity).

Introduction

Financial accounting concepts, often referred to as accounting principles or GAAP (Generally Accepted Accounting Principles), are a set of fundamental guidelines that govern the field of accounting. These concepts provide a structured framework for recording, reporting, and interpreting financial transactions, ensuring consistency, accuracy, and transparency in financial statements.

A central concept in accounting is the Accounting Equation, which forms the foundation of the double-entry accounting system. This equation explains how business resources are financed and ensures that financial records remain balanced. The accounting equation is expressed as:

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$

This principle underlies all accounting records and financial statements. Understanding it helps in interpreting financial data and managing business resources effectively.



2. Literature Review

Several accounting scholars and professional bodies emphasize the importance of the accounting equation as the backbone of financial accounting. Weygandt, Kimmel, and Kieso (2019) describe the accounting equation as the structural basis of

accounting, ensuring each transaction maintains balance through dual effects. They argue that understanding the equation helps users comprehend financial statement preparation.

Horngren et al. (2018) note that the equation explains how assets are financed either through owner investment or external borrowing. Their research also highlights the continued relevance of this principle despite technological advancements in accounting systems. The International Financial Reporting Standards (IFRS) framework recognizes assets, liabilities, and equity as fundamental elements of financial statements, reinforcing the accounting equation's importance.

3. Methodology

This study adopts a descriptive qualitative approach based on secondary data sources. The methodology includes:

- Reviewing accounting textbooks, academic journals, and professional accounting standards.
- Conceptual analysis of accounting principles and financial reporting frameworks.
- Use of practical examples to explain how the accounting equation operates in real business situations.
- Examination of accounting practices used in organizations. This method focuses on theoretical understanding rather than primary empirical data collection.

4. Fundamental Concepts of Accounting

Assets

Assets are economic resources owned or controlled by a business that provide future benefits. **Examples** include:

- Cash
- Inventory
- Machinery
- Buildings
- Accounts receivable

Assets are classified as:

- Current assets (cash, inventory, receivables)
- Non-current assets (land, buildings, equipment)

4.2 Liabilities

Liabilities represent obligations or debts a business owes to external parties.

Examples include:

- ✓ Bank loans, Accounts payable
- ✓ Salaries payable, Taxes payable

Liabilities are divided into:

- ✓ Current liabilities (short-term obligations)
- ✓ Long-term Liabilities

4.3 Owner's Equity

Owner's equity represents the owner's residual interest in the business after liabilities are deducted from assets. It includes:

- ✓ Capital invested by the owner
- ✓ Retained earnings
- ✓ Owner withdrawals (drawings)

Equity increases through profits and investments and decreases due to losses and withdrawals.

5. Application of the Accounting Equation

Each business transaction affects at least two components of the accounting equation while maintaining balance.

Example 1: Owner **invests** \$5,000 cash.

- ✓ Assets increase (cash) Owner's equity increases

Example 2: Equipment purchased using a **bank loan**.

✓ Assets increase (equipment)

Liabilities increase (loan)

Example 3: Payment of expenses in cash.

✓ Assets decrease

Owner's equity decreases

Thus, the accounting equation always remains balanced.

6. Importance of the Accounting Equation

The accounting equation is important because it:

- ✓ Forms the basis of double-entry bookkeeping.
- ✓ Ensures accuracy in financial records.
- ✓ Supports preparation of financial statements.
- ✓ Helps managers and investors understand financial structure.
- ✓ Promotes transparency and accountability.

Conclusion

The accounting equation is the foundation of accounting practice and financial reporting. It explains the relationship between assets, liabilities, and owner's equity, ensuring financial records remain accurate and balanced. Understanding this equation is essential for businesses, accounting students, and financial professionals, as it supports effective financial management and informed decision-making.

Discuss the role of financial accounting in business decision-making, highlighting the importance of financial statements.

Financial accounting is a way to keep track of money coming in and going out of a business and how those transactions are summarized and reported. It handles crucial financial data. Financial accounting is a function in any company, but more value could be extracted if truncation was better managed. Regarding organizational and social factors, researchers are still trying to pinpoint the significance of financial accounting. Aspects of financial accounting quality can be impacted by efforts to standardize and harmonize the practice nationally (Hopwood, 2000).

Managing and making business decisions across international borders can sometimes take time and effort. Many nations are continually revising and upgrading their rules and regulations to bring financial management on a global scale, which helps to make international business decisions easier. Keep up with the quality of your accounts while staying in line with the newest legislative revisions. This is a common challenge for accountants due to the regular policy updates. Because of this, the reliability of the data derived from the financial accounts suffers

Accounting plays a crucial role in business decision making. It provides essential financial information that helps business owners and managers make informed decisions about how to allocate resources, set pricing and plan for the future. In this blog post, we at MGI Worldwide will explore the role that accounting has in business decision making.

Performance Evaluation:

Enables stakeholders to track progress against goals, analyze trends, and identify areas for improvement.

Resource Allocation:

Helps managers determine where to invest capital to maximize efficiency and returns.

Strategic Planning & Forecasting:

Uses historical data to create projections for future performance and potential risks.

Transparency & Credibility:

Provides accurate, standardized information to external stakeholders (investors, regulators) for decision-making regarding investments or lending.

Compliance:

Ensures adherence to legal and regulatory requirements, including tax obligations. Accounting is important for regulatory compliance. Businesses are required to comply with various laws and regulations, such as tax laws and financial reporting requirements. Accounting provides the necessary financial information to ensure these regulations are followed.

Financial information:

One of the primary roles of accounting is to provide accurate financial information. This information includes income statements, balance sheets and cash flow statements, which give a clear picture of a company's financial health. Business owners and managers can use this information to assess the financial performance of their company, identify areas for improvement and make decisions about investments and expenditures.

Decision making:

Another important role of accounting in business decision making is to help with financial forecasting. By analysing historical financial data, businesses can make informed predictions about future financial performance. This information can help business owners and managers set realistic goals, identify potential risks and plan for the future.

Pricing decision:

Accounting also plays a critical role in pricing decisions. By understanding the cost of producing goods and services, businesses can set prices that are competitive while still allowing for profitability. Accounting information helps businesses determine the direct costs of producing goods or services, such as raw materials, labour and overhead costs. This allows businesses to make pricing decisions that take into account their costs and the market demand for their products or services.

Examine the key principles underlying accounting practices, such as accrual accounting, the matching principle, and the revenue recognition principle.

Key Principles:

It is based on the matching principle, where revenues are recorded for the period when goods and services are delivered, and expenses are recorded when goods and services are purchased (thereby matching revenues earned against expenses incurred during the same accounting period).

Here is a detailed examination of these key principles:

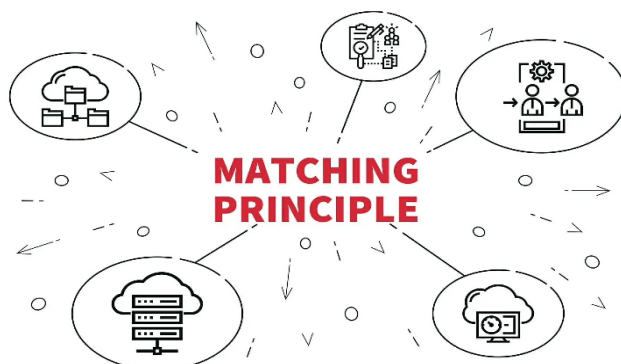
Accrual Accounting:

This foundational method records revenue and expenses in the period they are earned or incurred, regardless of when cash changes hands. It offers a more accurate picture of a company's assets, liabilities, and profitability than cash accounting.

Revenue Recognition Principle:

A critical component of accrual accounting, this principle dictates that revenue is recognized when it is earned, not necessarily when cash is received. It requires that goods/services are delivered and it is probable that payment will be received.

Matching Principle:



This principle requires that expenses be recognized in the same period as the related revenues they helped generate. It links expenses directly to revenue, ensuring that profitability for a specific period is not distorted.

Matching Principle			
Assumptions		Financial Statements	
Salary Information		Income Statement	2018
2018 Revenue	\$100	Revenue	\$100
Annual Bonus %	5%	Cost of Goods Sold	(\$25)
2018 Bonus Value	\$5	Gross Profit	\$75
2018 Bonus - Date Paid	15-Feb-19	Marketing	(\$7)
		Depreciation	(\$12)
		Salaries	(\$15)
		Bonuses	(\$5)
		Taxes	(\$4)
		Net Income	\$32
		Balance Sheet	2018
		Cash (current asset)	\$5
		Bonuses Payable (current liability)	\$5

Key Takeaways:

Focus on Timing: Accrual accounting ensures revenue and expenses are recognized when they occur, not when cash is moved.

Consistency:

These principles (along with consistency, cost, and materiality) are essential for GAAP and IFRS compliance, providing transparent financial reporting.

Improved Accuracy:

Together, these principles prevent the manipulation of earnings and provide a better understanding of a company's financial health.

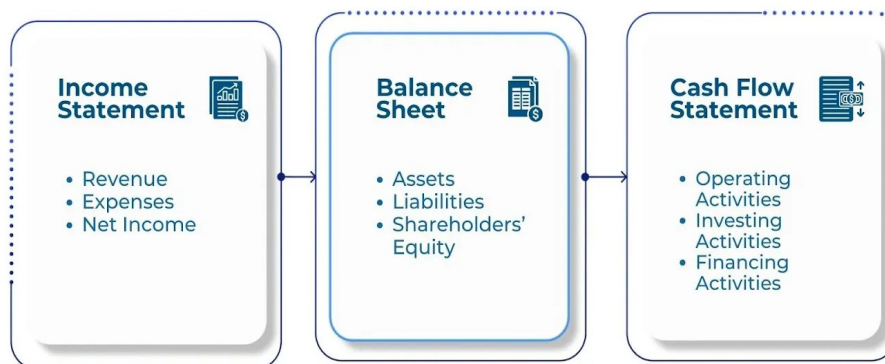
Analyze the relationship between the balance sheet, income statement, and cash flow statement.

Relationship

Financial statements are essential tools for understanding a company's financial health and performance. The three primary financial statements—the Balance Sheet, Income Statement, and Cash Flow Statement—are interconnected and provide different but related perspectives on a business's financial position.

Understanding the relationship among these statements helps users interpret how a business earns profit, manages assets and liabilities, and generates cash.

Types of Financial Statements



1. Balance Sheet

The Balance Sheet shows a company's financial position at a specific point in time. It summarizes what a company owns and owes. The Balance Sheet is a snapshot of a company's financial health at a specific time. It's divided into three key sections: assets, liabilities, and shareholders' equity. These components offer a clear picture of what a company owns, what it owes, and the value left for its shareholders.

It is based on the accounting equation:

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$

Components include:

Assets: Cash, inventory, property, equipment, receivables.

Liabilities: Loans, accounts payable, and other obligations.

Owner's Equity:

Capital invested and retained earnings.

The balance sheet represents a snapshot of financial health on a specific date.

2. Income Statement

The Income Statement, also called the **Profit and Loss Statement**, shows company performance over a period of time. It measures **profitability**. The Income Statement is like the report card for a company's performance over a specific period. It shows whether a company is profitable by comparing its revenues to expenses.

The statement outlines revenue, cost of goods sold, gross profit, operating expenses, and net income. These components tell a clear story of how much money came in and how much was spent, leading to either a profit or a loss.

Key components include:

- ✓ Revenue or sales
- ✓ Cost of goods sold
- ✓ Operating expenses
- ✓ Profit or loss

The final figure is net income, which shows whether the company made a profit or loss during the period.

3. Cash Flow Statement

The Cash Flow Statement reports actual cash inflows and outflows during a period. It shows how cash is generated and used. The Cash Flow Statement is crucial for assessing a company's liquidity and financial flexibility. Unlike the Income Statement, which includes non-cash items, the Cash Flow Statement focuses solely on actual cash inflows and outflows during a period. It categorizes these cash flows into three main sections: operating activities, investing activities, and financing activities.

Cash flows are **grouped** into:

1. Operating activities (daily business operations)
2. Investing activities (purchase or sale of assets)
3. Financing activities (loans, investments, dividends)

It explains changes in the company's cash position.

4. Relationship Between the Three Statements

These statements are interconnected and cannot be fully understood in isolation.

a) Income Statement and Balance Sheet

Net income calculated in the income statement affects the balance sheet through retained earnings, which are part of owner's equity. If a company earns profit: Retained earnings increase. Owner's equity increases on the balance sheet. If the company makes a loss: Equity decreases.

Thus, income statement results directly impact the balance sheet.

b) Balance Sheet and Cash Flow Statement

The cash flow statement explains the change in cash balance between two balance sheet dates.

Beginning cash balance + net cash flows = ending cash balance. Thus, cash reported in the balance sheet equals the final cash figure in the cash flow statement.

c) Income Statement and Cash Flow Statement

Net income from the income statement is the starting point for calculating cash flows from operating activities. However, net income includes non-cash items such as depreciation and credit sales, so adjustments are made to calculate actual cash flow.

d) Combined Relationship

1. Income statement shows profitability.
2. Profit increases retained earnings in the balance sheet.
3. Cash flow statement explains how cash moved during the period.
4. Ending cash appears on the balance sheet.

Together, they show performance, financial position, and liquidity.

5. Example of Interconnection

Suppose a company earns profit of \$10,000: Income statement shows net

income of \$10,000. Retained earnings increase on the balance sheet. Cash flow statement shows whether profit was received in cash or credit. If customers have not paid yet, profit exists but cash may not increase.

7. Conclusion

The balance sheet, income statement, and cash flow statement are interconnected components of financial reporting. The income statement measures performance, the balance sheet shows financial position, and the cash flow statement explains cash movement. Together, they provide a complete picture of a company's financial health and operations.

Provide examples of how these concepts are applied in real-world accounting practices.

In real business environments, companies use the balance sheet, income statement, and cash flow statement daily to monitor performance, manage finances, and make decisions. These statements are interconnected and applied in practical accounting activities across industries

1. Example: Retail Business Operations

A clothing store records daily sales and expenses.

Application

Sales revenue appears in the **income statement**.

Inventory remaining appears as an asset on the **balance sheet**.

Cash received from customers is recorded in the **cash flow statement**.

2. Example' Equipment purchase:

If any company purchases any machinery which is worth \$20,000 through bank loan.

Application:

Equipment increases assets on balance sheet.

Loan increases Liabilities.

Cash flow statement records financing inflow and investing outflow.

3. Example: Credit Sales

A business sells goods worth \$5,000 on credit.

Application

Revenue appears in the **income statement**.

Accounts receivable increase on the **balance sheet**.

Cash flow statement shows no immediate cash inflow.

4. Example: Payment of Salaries

A company pays employees monthly salaries.

Application

Salary expense reduces profit in the **income statement**.

Cash decreases in the **balance sheet**.

Cash flow statement shows operating cash outflow.

Income Statement

Description	Amount (\$)
Revenue	30,000
Expenses	(10,000)
Net Profit	20,000

Cash Flow Statement

Activity	Cash Flow (\$)
Financing (investment)	+50,000
Investing (equipment purchase)	-20,000
Operating (sales – expenses)	+20,000
Net Increase in Cash	50,000

Ending cash = 50,000.

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Appendix

Appendix A: Accounting Equation Illustration

Transaction	Assets (\$)	Liabilities (\$)	Owner's Equity (\$)
Owner invests cash	+50,000	–	+50,000
Equipment purchased	+20,000 Equipment	–	–
Cash used for equipment	–20,000 Cash	–	–
Sales revenue earned	+30,000 Cash	–	+30,000
Expenses paid	–10,000 Cash	–	–10,000

Accounting equation maintained:

Assets = Liabilities + Owner's Equity

Appendix B: Sample Income Statement

Income Statement for the Year Ended

Description	Amount (\$)
Sales Revenue	30,000
Expenses	(10,000)
Net Profit	20,000