

PARROTT & PARROTT

OUR GUIDE TO YOUR BUSINESS ACCOUNTS



What exactly are Business Accounts?

“Statements of Finance” are probably a better description of a business’s annual or management accounts, which show profitability of a business or otherwise, together with a snapshot of the “Financial” state of affairs at a particular date. Depending on the type of business, legal status and use to which the financial statements will be put, determines the complexity and detail prepared to which the accounts are prepared.

The minimum accounts information would be :-

The Trading and Profit and Loss Account

This statement shows gross income generated by the business in the financial period, less direct costs of producing that income e.g. stock purchases for re-sale, delivery cost of items sold etc. to arrive at a Gross Profit. Administration and other overhead costs of operating the business e.g. rent, electricity, telephone etc. Depreciation costs for plant, equipment, fixtures and computer equipment are also provided to spread the costs of these items over their useful economic life. Costs relating to the finance of the business e.g. bank interest, hire purchase interest. The result of these items is the arrival at the “Net” pre-tax profit of the business.

For tax purposes adjustments may need to be made to this profit, in particular costs which may have a non-business element and special beneficial tax allowances for spreading the cost of asset purchases.

XYZ Limited Profit and Loss Accounts for the year ended 31st March 20XX

Sales		150,000	
Direct Costs		50,000	

Gross Profit		100,000	66%
<u>Overheads</u>			
Rent & Rates	5,000		
Light & Heat	980		
Motor Expenses	4,250		
Depreciation	500		

Total overheads		10,730	

Pre Tax Profit		89,270	
Corporation tax		16,960	

Net profit for the year		72,310	
Dividends paid		59,010	

Retained profit for the year		13,300	
		=====	

The Balance Sheet

Every business should also produce a balance sheet which gives a snapshot of the business's financial state at the date to which the accounts are made up. The balance sheet shows what monies are invested in the business by way of plant, machinery etc. Monies which the business is owed from its customers, monies which it owes to its suppliers, money held in the bank or owed to the bank in the case of overdrafts and loans. Monies owed to other creditors e.g. VAT, PAYE etc.

The net balance of these items reflects the "Net Worth" of the business and is represented by monies due to the business owners, whether as company profits not distributed to shareholders, profits not drawn by sole traders or partners and monies injected to the business by the owners e.g. share capital, sole trader or partner capital/current accounts.

In addition to the above minimum the "Financial Statements" may also include notes to the accounts giving further details or breakdowns of items contained in the Profit and Loss Account and/or Balance Sheet.

XYZ Limited Balance Sheet at 31st March 20XX

Fixed Assets		10,000
<u>Current Assets</u>		
Cash at bank	15,250	
Cash in hand	250	
Trade Debtors	28,500	
Prepaid expenses	750	

	44,750	
<u>Current Liabilities</u>		
Trade Creditors	4,650	
PAYE	450	
VAT	1,250	
Bank Loan	10,000	
Directors loan accounts	25,000	

	41,350	

Net current assets		3,400

		13,400
		=====
Share capital issued		100
Retained profits		13,300

		13,400
		=====

Why bother to prepare accounts?

There are many reasons for preparing accounts for your business, which are summarised below:-

- 1) Providing information for the owners of the business to assess the success of the business in terms of profits. Information to monitor the financial standing of the business, liquidity and future cash / asset requirements. This is of course the primary purpose of producing accounts.
- 2) Providing a sound basis from which to calculate tax liabilities for the business/owners. Properly prepared accounts from which these calculations are made are favoured by the Inland Revenue.
- 3) Satisfaction of legal obligations, this is especially true for Limited companies who must publicly file accounts with the Registrar of Companies. This is equally true for some professions whose regulators and professional bodies require annual submission of accounts.
- 4) Providing accurate financial information to potential investors, banks etc. to assess the creditworthiness of a business. In the case of Sole Traders and Partnerships the accounts may also be used to prove income to support mortgage applications etc.

Due to the variety of uses to which accounts are put, as can be seen above, it is essential that the information produced is accurate, otherwise wrong decisions could be made both by the business owner or by a third party. This could of course have serious implications for the business owner and in the case of items 2 and 3 above prosecution and fines could be the result of the inaccuracies.

How are financial statements prepared by Parrott & Parrott?

Initially when your books and records are brought into our offices or collected by our staff, we log the date received into our computer system. Your books are now in our "accounts production queue". We aim to process clients' accounts in the order that they are received and as quickly as possible after they are received. Obviously, we do have peak times when a lot of books and records are brought in e.g. March year ends and calendar year ends, at these times it may take longer than others to deal with the preparation of the accounts. To help us and yourself it is essential that the records are brought in as soon as possible after the end of your year end and not left to the last minute of filing deadlines. Under these circumstances we will NOT move you to the top of the queue as of course this only inconveniences other clients who have brought their books in to us in good time.

As far as the actual work of preparing the accounts is concerned, we have a work programme tailored to each client, which we follow. There are however basic procedures which we follow for all clients. The work programme ensures quality and consistency to our work regardless of the size of the clients' business.

To ensure the accuracy of information we produce, we carry out basic checks on your books and records to ascertain whether or not the information contained is numerically correct before we continue to analyse the books and records.

Much of this work is dependent on the type and quality of the information we receive from you, this also will dictate the amount of time we need to spend on your accounts. We can generally split down the type of information we receive into the following categories:-

Styles & Types of Book & Records

1) Computerised accounts.

These are generally the easiest way for us to deal with your affairs as the majority of software forces the user to agree the bank balances, debtors and creditors as they go. However, there are some software packages which although sold as “book-keeping” products are very poor and should NOT be used to run the book-keeping for any business. Before purchasing and changing your business accounting records to a computerised system please check with us as to the suitability of the software, this could save you considerable aggravation and cost later on!

2) Manual Cash Books

Well written and accurate cash books are still the best alternative to computerisation. It is essential that the books are written up in a way that allows us to extract necessary information without the need to nearly re-write the books to get at the detail we need. It has been known on more than one occasion that a client has presented us with beautifully written up books but we have had to start from scratch as the information was in a completely useless format from which to prepare accounts. This can lead to very expensive bills which could of course have been avoided.

3) “Nightmare” – The Supermarket Bag

No more really need be said about this, other than that the cost of producing accounts from bits of paper with no cross reference to bank statements/cheques/paying in books etc. is normally very high, as you would imagine, it is very labour intensive. Not only are there cost implications but should the Inland Revenue decide to look at the finances of the individual concerned it is usually nigh on impossible to prove income accurately and the Revenue will then simply penalise the tax payer.

Regardless of the business’s status i.e. Sole Trader/Partnership/Limited Company there is a legal requirement for the business owner to maintain “Proper Books and Records”. In the case of Limited Companies failure to do so can lead to fines and in the worse case scenario a holiday at Her Majesty’s pleasure.

The Inland Revenue also require that businesses maintain proper books and records. Whilst they may not fine for non-compliance they will make life very difficult and could lead to a business paying more tax than was actually necessary, had accurate books been maintained.

Information we need from you

As well as records of transactions we will also need the following information and documentation:-

- a) All bank statements covering the year or period of the accounts. It is essential to have a statement that covers the period end date.
- b) Details of any cash floats or un-banked monies at the period end.
- c) All expense and purchase invoices and receipts.
- d) Details and/or copies of new finance agreements during the period e.g. leases, hire purchase, bank loans etc.
- e) All sales invoices issued.
- f) A detailed list of monies owed to the business by customers. A note of any bad or potential bad debts.
- g) A detailed list of monies owed by the business to suppliers or service providers.
- h) Detailed list of stock at the period end.
- i) Details of any work done or goods supplied not invoiced at the period end.
- j) A note of any assets purchased or sold in the period if not easily identified from the records supplied.
- k) A note of any unusual items sold, purchased or matters which may have affected the business.
- l) All payroll records covering the period and copies of any P35 or P11D sent to the Inland Revenue.

Our Accounts Preparation Procedures

Generally we follow the following steps when preparing the business accounts:-

- 1) Prove and reconcile the business bank account/s
- 2) Prove and reconcile the Trade Debtors (monies owed to the business)
- 3) Prove and reconcile the Trade Creditors (monies owed by the business)
- 4) Extract and re-analyse costs and income into the Profit and Loss format relevant for the type of business
- 5) Analyse wage and salary records (where appropriate) to extract Directors wages, national insurance and ensure the PAYE owed at the end of the financial period is correct
- 6) Verify and reconcile the VAT position at the end of the financial period. This will also involve reviewing all VAT returns made in the financial year/period
- 7) Obtain and check invoices for asset additions e.g. plant and machinery, motor vehicles etc.
- 8) Calculate depreciation on each individual asset and balance of asset value
- 9) Review and if necessary calculate profits and losses on sale of assets
- 10) Detailed review of items in the profit and loss account to ensure only genuine business expenses are included. It may seem a good idea to put through private/non-business expenses through the business but these will only need to be removed to ensure accuracy.
- 11) Review expense items which may have been paid in advance e.g. insurances, deposits etc. Make necessary allowances for costs which have been incurred during the period but not billed until after the end of the year. These adjustments are called prepayments and accruals and are made to match accurately costs against income.
- 12) Where necessary review stock of materials for re-sale and/or Work in Progress
- 13) Compare in detail the current period income and expenses with the previous period. This is to highlight and potential inaccuracies and exceptional items which occurred in the period. This is exactly the review carried out by the Inland Revenue and discrepancies can lead to them starting an enquiry/investigation – forewarned is forearmed.
- 14) Review owners' drawings and where necessary analyse e.g. personal pension payments etc. In the case of Limited Companies Directors salaries, loan accounts and dividends.
- 15) Prepare calculations of business profits for tax purposes and in the case of Limited Companies calculating Corporation Tax liability which is then included in the accounts.
- 16) Review the business payroll and correctly analyse gross pay and employers national insurance to arrive at the cost to the business of employees. Extract

sufficient information to determine any outstanding PAYE balance at the period end.

- 17) In the case of Limited Companies, prepare and reconcile schedules of Directors remuneration.
- 18) Extract sufficient information from the books and records to prepare Inland Revenue forms P11D – Expenses and Benefits Returns for Directors and Employees.
- 19) Once draft accounts have been prepared these are reviewed by a senior member of staff and any problem areas identified and if necessary contact the client to discuss these. If amendments are required these are processed e.g. dividends, staff bonuses etc.
- 20) In the case of Limited Companies, Corporation Tax calculations are prepared to determine taxable profits and the liability to taxation. The liability is then incorporated into the accounts.
- 21) For sole traders and partnerships, calculations are made to determine the taxable profits of the business for incorporation into either the Partnership Tax Return and/or the individual taxpayers Self Assessment Tax Return.
- 22) Accounts are then sent to the business owner/s with a covering letter explaining any points in the accounts which need to be raised. Alternatively, a meeting with the client may be arranged to go through the accounts in some detail and discuss any problem areas or future plans etc.
- 23) Finally, after the accounts are approved and signed, they are lodged with the various statutory bodies as required e.g. Companies House and Inland Revenue.

The amount of involvement and interaction with our client does depend entirely on individual circumstances and how much advice the client requires in relation to their business. It is always possible to make an appointment to discuss any matter relating to the business, accounts, taxation or book-keeping, please just make a phone call.

At Parrott and Parrott we do pride ourselves on preparing accurate and meaningful accounts and following the steps above we hope to ensure this is the case. We also have a good relationship with the Inland Revenue who we are sure, know that we strive to produce accurate accounts and tax returns and this of course reduces the chances of them making enquiries into returns.

Over the years we have taken on many jobs from other accountants who do not necessarily spend as much time as is necessary to produce accurate accounts and more often than not this is reflected in the price being charged for the work carried out and subsequent Inland Revenue activity. We do try to provide a professional service where the job is done thoroughly. We can of course only be as good as the information supplied to us, this is your responsibility. Whilst we do prepare the accounts we do so only as your agent, the accounts are still YOURS. It is essential that you let us know ALL the information relevant to the finances of the business and that the books you use to record the business activity are correct and in a sensible format. We would rather you ask about any accounts query or other finance matter at the time it occurs rather than some 12 months or more later when we are dealing with your accounts. It is not often that matters can be rectified after the event !

Does and Don'ts With Your Business Accounts

To help us and yourself there are several things you can do which will keep our time down on work carried out, which will of course lead to lower accountancy bills for you:-

- 1) Keep ALL personal and business monies separate.
- 2) In the case of sole traders and partnerships it is essential that a separate business bank account is operated. This may mean you do incur some bank charges but these will be minimal in comparison to the extra time involved on our part and possibly that of the Inland Revenue. If the bank charges seem excessive try another bank, do not feel obligated to stick with a bank you have used all your life !
- 3) In the case of Limited Companies – NO personal bank accounts should ever be used. It could be deemed that any income going into this type of account is yours personally and yes, you would be taxed on it accordingly!
- 4) Sole trader/partnership bank accounts must only be used for business income and expenses. We recommend Drawings are made in round sum amounts e.g. £100, £1,000 etc. and paid into your personal bank account. Also, try and keep the volume of this type of transaction to a minimum, say once a month. If you are not sure if an expense is “allowable” for business purposes please ring us BEFORE you put it through the books. In addition, not putting through personal items will reduce the amount of time you spend on your book-keeping and of course on the amount of time we would need to spend on analysing your records. Another problem can also arise if business monies are used personally, in that small amounts soon mount up over the period of a year and as we have seen all too often, the drawings from the business exceed the profits!
- 5) Limited Company Directors drawings/dividends. As above keep the number of transactions to a minimum and again round sum amounts. Please also bear in mind that Dividends can only be paid from a company's After Tax Profits. Do not assume that if there is cash in the bank that this must be profit ! Excess drawings will lead to your Directors loan account being overdrawn and the Inland Revenue will charge a flat rate tax of 25% on these amounts. It is also contrary to the Companies Acts and could get you into serious trouble.
- 6) Above all make sure you retain all receipts and proof of expenses/costs incurred, not only for the business but also your personal expenditure. Without the piece of paper for business expenditure you cannot prove the expense and the Inland Revenue will just assume you had the money personally and tax you accordingly or merely disallow the expense which could lead to a higher tax liability.
- 7) Credit cards. Sole trade and partnerships obtain a card for use only as a business facility. Try and avoid using switch cards, this normally leads to far more transactions going through the bank than is necessary, use the credit card and make one payment through the bank a month. Also the point 4. above is equally valid for credit cards.

- 8) Credit cards. Limited companies. Do not settle credit cards in personal names with company cheques, even though all the items may well be business. Put an expense claim into the company, this need only be a piece of paper written out as such. The expense payment should then be dealt with through your personal account. In this way the Limited company has not “settled” your personal liability with the credit card, as this is TAXABLE !
- 9) Ensure that all invoices issued for sales or work done show a sequential invoice number, date the work or supply was made, and the customer name and address.
- 10) Any entertaining carried out (NB this is not an allowable business expense) may be claimed but ensure that the receipt etc. shows who you were entertaining.
- 11) Ensure you receive printed bank statements for the business account from your bank at least monthly. Check the statements to ensure that your books have the same entries, it is easy to miss direct debits etc. Use the statements to “prove” your books and bank balance. Banks do make mistakes and unless you check you will not know !

If the outline of record keeping and guidelines above are followed it is far easier for us to prepare your accounts and ensure that they are accurate and meaningful. It will also help in any potential dealings with the Inland Revenue. Once again, if you are unsure about any aspect of the record keeping or what you can or cannot claim by way of expense please contact us for advice.



PARROTT & PARROTT
INCORPORATED FINANCIAL ACCOUNTANTS
OUR STAFF & CONTACT DETAILS

Steve Parrott	-	Principal & director Business and Personal Taxation advice and planning Business accounts, cash flows Budgeting and business advice	-	steve@parrott.co.uk
Jackie Parrott	-	Administration director Client Book-keeping	-	jackie@parrott.co.uk
Sue Showler	-	Accounts production Payroll & PAYE advice Book-keeping advice VAT advice	-	sue@parrott.co.uk
Angela Fleet	-	Accounts production Book-keeping advice VAT advice	-	angela@parrott.co.uk
Sue Darke	-	Accounts production Client Book-keeping	-	suedarke@parrott.co.uk
Lisa Parrott	-	Practice Co-ordinator Client Payrolls Contact for appointments	-	lisa@parrott.co.uk
Sheila Milsome	-	Secretary Contact for appointments	-	sheila@parrott.co.uk
Office Phone:		01548 853053		
Office Fax:		01548 856062		
Website:		www.parrott.co.uk		
Office Hours:		9:00am to 5:00pm Monday to Friday		

