# A Guide to Accounting by Rise

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*Disclaimer: The information provided in this accounting guide is for general information purposes only. Rise accounting tips are provided for informational use only. The steps to set up accounting books presented in this guide should be considered recommendation only. Different business industries and stages of business development may require other steps. Consult a professional bookkeeper or accountant before making any business decisions. Please always consult with an accounting professional.*

## Checklist



## Steps to set up books

### 1. Determine your fiscal year

A fiscal year is a 12-month financial reporting period for a business.

- For sole-proprietorships and partnerships, it is usually a calendar year (January 1 - December 31). It might be changed by applying to CRA (Form T1139).
- Corporations can choose a fiscal year-end within 53 weeks of their incorporation date. The year-end date is set when the first tax return is filed. Many corporations choose fiscal year-end when sales and inventories are low.

### 2. Open a business bank account

Separating personal and business funds/expenses is a good and easy way to make sure that financial transactions are recorded accurately for the purposes of analyzing, reporting, and filing income tax.

- **Sole-proprietorships and partnerships**
  Banks and financial institutions offer special business bank accounts. While it is recommended to have a business bank account, it is not always affordable for new business owners. If a business bank account is not an option, a sole proprietor may open a separate personal account and use it exclusively for business transactions (sales and purchases). With the increase in online shopping, make sure that your account has a debit/credit card for online purchases.

- **Corporations**

A corporation is considered a separate legal entity. That is why a business bank account must be opened for an incorporated business.

Research different options of opening a business bank account or separate personal account. Note that fees vary depending on banks and types of accounts. Consult with your bank on what documentation is needed.

### 3. Choose an accounting method

Two types of accounting methods:

- **Cash method**
  Report income when you receive it and deduct expenses when you pay them. This method is available for farmers, fishers and self-employed commission employees.

- **Accrual method**
  Report income when you earned it (not when you received it) and deduct expenses when you incur them (not when you paid them). This method is used for all other types of businesses in Canada.

### 4. Determine how you will record transactions

- **Manual system**
  Manually record business transactions in a book or spreadsheet.

| Pros | Cons |
|---|---|
| + Free or cheap (There are lots of free bookkeeping templates that can be used for manual bookkeeping.)<br><br>+ Great for businesses with a small number of transactions. | - Minimal reporting options and automation.<br><br>- May take more time, especially if you grow your business and the number of transactions increases rapidly. |

- **Accounting software**
  Two types of accounting software are traditional desktop and cloud-based.
    - **Traditional desktop software** requires installation on the hard drive of your computer. It does not require internet access and is considered more secure. It usually costs more than cloud-based, and you can only access it from the device on which it is installed.
    - **Cloud-based software** has become more and more popular for its convenience. It can be accessed from different devices through an internet connection (laptop, cell phone, etc.), and more than one person can access the software. For example, a business owner can allow a bookkeeper to access the company's transactions and information to work on them together. The cloud-based solution is cheaper than desktop solutions, but as with everything that is internet-based, it is not as secure as the traditional software you install.

Accounting solutions are used for invoicing clients, recording transactions, and generating and reviewing financial reports.

Some examples of cloud-based solutions:

- QuickBooks (https://quickbooks.intuit.com/ca/). There is also a desktop option.
- Freshbooks (https://www.freshbooks.com/) Rise clients can receive two-months free (https://www.freshbooks.com/education/rise-smallbusinesslending?ref=12789)
- Wave (https://www.waveapps.com/)
- Sage (https://www.sage.com/en-ca/). There is also a desktop option.
- Xero (https://www.xero.com/ca/)

| Pros | Cons |
| --- | --- |
| + Includes invoicing and may be connected to a bank account to streamline bookkeeping and save time.<br>+ Available from multiple devices (laptop, cell phone).<br>+ Financial reporting is available to help you understand how your business is doing.<br>+ There is some protection from making accounting errors. | - Although some solutions are free, most of them charge monthly fees depending on the software and options included.<br>- Requires an initial time commitment for software set up and training.<br>- Easy to make mistakes at the beginning if not set up well. |

- **Bookkeeper/accountant**

Hire a bookkeeper or accounting firm to do your books, financial reporting and tax returns.

| Pros | Cons |
| --- | --- |
| + Bookkeeper can take responsibility for transaction recording, sales, and income tax filing and reports preparation.<br>+ The time you previously spent on bookkeeping, can now be spent to grow and develop your business.<br>+ Increased protection from accounting errors. | - Can be expensive depending on the services provided.<br>- There is a possibility that you may lose track of income, expenses, and understanding the financial side of your business. Regular review of financial statements is needed.<br>- Bookkeeping is an unregulated profession. Ask about any bookkeeper's experience and education to avoid dishonest and unqualified bookkeepers. |

## 5. Set up a chart of accounts

A chart of accounts is a list of all accounts used in the accounting system by a company. When a transaction is recorded, it is categorized according to the chart of accounts.
The chart of accounts is usually organized into five sections:

1. **Assets**
   Items of value owned by a company (cash, accounts receivable, inventory, prepaid expenses, equipment, vehicles, etc.)
2. **Liabilities**
   Debts or obligations of a business (accounts payable, loans payable, company's credit card, HST, etc.)
3. **Equity**
   Owner's contributions (Capital) and withdrawals
4. **Revenue**
   Service revenue/sale of products
5. **Expenses**
   Cost of goods sold, supplies, rent, utilities, advertising, depreciation, interest, wages, etc.

The chart of accounts should be customized to suit your business activities. It should also be changed when the business grows and additional accounts are needed.

## 6. Set up a schedule that reflects an accounting cycle of your business

Bookkeeping is an ongoing part of the business. Create a schedule that suits your accounting cycle to ensure that you do not fall behind on your books.
Depending on the type of business (retail, services, manufacturing, etc.), you may need to work with your records daily, weekly, biweekly, monthly. For example, a retail location may benefit from

recording sales and expenses daily, while a web designer may need to record transactions weekly or monthly.

Generally, the schedule may look like this:

At the start:

- Set up an inventory tracking system. You can do it manually or using the software. Record the beginning inventory.
- Start a list of assets brought into the business at start-up.
- If you use your vehicle, record the odometer reading in the car and set up a mileage log to record kilometers driven for business use.
- Track your revenues and expenses, including cash transactions daily to check your cash position.  Record each transaction daily or weekly depending on the volume (accounting software helps make this process faster).
- Keep physical copies of your receipts in a folder, scan, or take a picture of receipts and store them in a computer folder together with electronic receipts/invoices. Sort them by month.
- Review unpaid bills and invoices.
- Don't let unrecorded receipts or records of sales pile up.

Monthly:

- Reconcile bank account with books to find and correct any mistakes.
- Reconcile credit card account with books to find and correct any mistakes.
- Review overdue invoices and send reminders to clients.
- Review inventory (if applicable) to ensure you are not short or overloaded.
- Review income statement and cash flow statement. Compare your results with the previous months to see the spending and earning trends.

Quarterly:

- Review financial statements. Compare and analyze your quarterly results.
- If your business is GST/HST registered, you may need to make quarterly sales tax payments.
- Estimate income tax to be paid. You can opt to do quarterly income tax installments.

Yearly:

- Review overdue accounts receivable and payable to identify accounts for follow-up and write-off. Reconcile book amounts with invoices and records.
- Count inventory as of December 31 to determine the value of items sold.

- Create a list of assets purchased during the year and calculate depreciation (recommended to use the CRA depreciation classes and allowable rates).
- Take odometer reading of vehicle used for business on December 31.
- Make adjusting entries (e.g. account for prepaid expenses, home office expenses, depreciation of equipment, etc.)
- Prepare or use software to generate financial statements: income statement, balance sheet, statement of equity, cash flow statement.
- Use information from financial statements to prepare for tax filing. Complete form T2125 for sole proprietorships and partnerships and T2 for corporations.
- Review and analyze the financial results for the year.

*Note: the schedules above do not include any payroll activities. They will depend on the conditions of employment: how often the employees are paid (weekly, biweekly, semi-monthly) and if employees are paid hourly or a salary. The timing of payroll activities may vary, but usual activities would include:*

- Maintain and update employees' records.
- Track and record employees' hours for hourly-paid employees.
- Prepare and run payroll manually or using the software. Calculate the amount of wages, EI, CPP, WSIB, vacation, tax, benefits, etc.
- Remit EI, CPP and tax withheld from employees' paycheck and employer's portion of EI and CPP. Know your remittance date (usually due to the 15th of the following month).
- Prepare T4s for employees at the year-end and T4 summary for CRA. Due by the end of February each year.

Items to review on a regular basis

Having cash (money in the bank account) is vital for the business. Check your cash position often to ensure you have enough to cover your operations.

Two types of accounts that may be confused with actual money on hand are accounts receivable and accounts payable.

- **Accounts receivables** occur when you perform service or sell goods, but clients have not paid yet. Essentially you sell goods/services on credit. Normally business needs to set the terms that require payments due within a certain time (e.g. due within 30 days). If your company provides such terms, you need to make sure that receivables are collected on time. If account receivables are overdue, reach out to clients with reminders of balance.
- **Account payables** occur when you purchase inventory, supplies or services but do not pay right away. It is a debt or obligation that needs to be paid within a certain timeframe (e.g. 30 days). If your suppliers provide such terms, use them with caution. Set a reminder or notification to pay the bill on time. Some suppliers offer a discount if you pay ahead of time.

Check if your suppliers do (e.g. 2% in 10, which means you receive a 2% discount if you pay during the first 10 days).

Review accounts payable and receivable to ensure that you receive money from your clients and pay your obligations.

### When to engage bookkeeper and accountant

Bookkeeping means recording everyday financial transactions (purchases, payments, sales) of the business manually or using the software. A bookkeeper is a person who may manage books, record daily transactions, complete the bank and credit card reconciliations, remit GST/HST returns and payments, run payroll, and compile data for year-end reports. Bookkeeping services may be customized depending on your business needs.

Accounting includes bookkeeping but also involves an analysis of the financial reports that help with business decisions.

The option of hiring someone to do the financial side of the business may sound attractive, but unfortunately, not many businesses can afford to hire a bookkeeper or accountant at the beginning. It is also essential for an entrepreneur to not only produce and sell their product/service, but to also understand the numbers behind the business start-up and operations. That is why it is good when a business owner is involved in setting up books, recording transactions and reviewing reports during the first stages of running the business.

There are several times when it might be beneficial to consult or hire a bookkeeper:

- To set up a bookkeeping system, especially if you decide to choose accounting software to use. The setup is important for the correct functioning and recording. Consider the consultation with a bookkeeper to receive answers to your questions and avoid mistakes in setting up books.
- Filing a personal tax return when you are self-employed or a tax return for a corporation requires some additional knowledge and understanding of tax regulations. It might be a great idea to consult an accountant at this point.
- When the business grows and the number and complexity of operations increase (e.g. payroll, GST/HST filing), it may be time to think about hiring a bookkeeper on a regular basis.

Accountants provide financial services to businesses on a level higher than everyday bookkeeping. When the company is set up, operates successfully, and shows stable income, an accountant may help you look at the financial statements to see the bigger picture of where the business can grow further. They provide financial advice on the stages of incorporation, hiring employees, opening new ventures, changing business strategy, etc.

If hiring a bookkeeper or accountant is not an option, there are many accessible and more affordable options for small business owners to receive this kind of support. Some resources may be found on official federal and provincial government websites, or through organizations that help small business owners and entrepreneurs, such as Rise.

There are multiple paid and free courses and guides on bookkeeping online as well. A great resource is https://www.accountingcoach.com/accounting-basics/outline. It provides information on basic accounting and bookkeeping processes.

## Ethics

Ethics are based on the value system that helps to differentiate right from wrong. Business ethics includes producing safe, quality products, treating customers responsibly, and understanding the business's impact on the environment, employees, community, etc.
Ethical issues may arise when dealing with business bookkeeping and accounting. It is a moral obligation of a business owner to make sure the business stays ethical and compliant, recording operation activities truthfully and correctly according to the provincial and federal accounting regulations.

The concepts of acceptable accounting practices are called generally accepted accounting principles (GAAP). In Canada, the Accounting Standards Board has issued a set of Accounting Standards for Private Enterprises that employ GAAP.

GAAP's primary purpose is to ensure that financial reports are faithfully represented, relevant for the users, are comparable, verifiable, timely and understandable. Such small things as making sure that daily transactions are recorded correctly, error-free and truthful will ensure that financial reporting is done within GAAP.

It is also a moral decision of the business owner to report true profits in a tax return and pay appropriate taxes that support the community and Canadian people through various government services. Refusing to file a tax return may result in the inability to use government services or seek financing (grants and loans). It may also be viewed as tax evasion, which has more drastic consequences.

The CRA audit system is working to reveal dishonest profit reporting and mistakes. Intentional under-reporting of income and over-reporting of expenses can be charged as fraud which results in fines and/or jail time. The unintentional errors that the CRA reveals in an audit will result in correcting tax information and paying more tax or receiving a refund depending on the situation but will not be viewed as fraud.

Business ethics means that every business owner makes the decision to either be honest and compliant with accounting and tax regulation or face the consequences.