

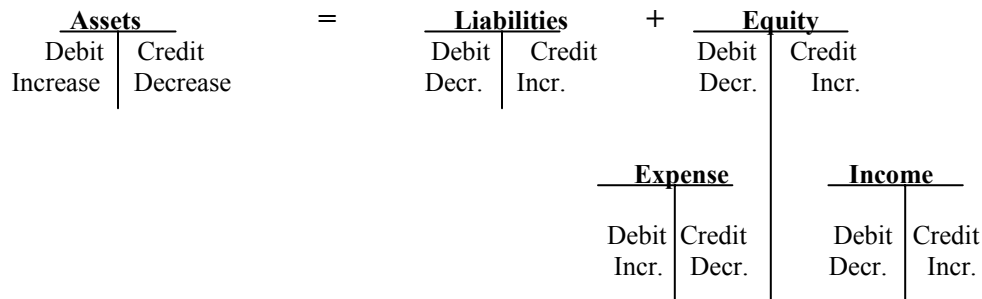
Study Guide for Advanced Accounting Entries

Introduction

The chart of accounts that you have setup for your business is an integral part of any accounting package. Through these accounts, you track the flow of money in your business. It tells you how much money you have, how much money you owe, where money is being spent, and how much money is coming in. Transactions will fall under the following types of accounts: assets, liabilities, equity, income, or expense. When coding your daily business, transactions will increase or decrease these types of accounts. A group of accounts used by a business in recording transactions is called a ledger. The specific accounts used by a business in recording its transactions vary from one concern to another. In other words, your chart of accounts is unique to your business and may not be the same as your neighbor's.

When recording your transactions, the mechanics of double entry comes into play. Every transaction affects two or more accounts with equal debits and credits. Transactions are so recorded because equal debits and credits offer a means of proving the recording accuracy. Running the trial balance in your accounting software shows equal debits and credits and is proof of your work.

Are debits and credits a little “fuzzy” to you? Let’s review. Remember the basic balance sheet formula: Assets equals liabilities plus equity. Here is how debits and credits affect this equation.



The terms “to debit” and “to credit” should not be confused with “to increase” and “to decrease”. To debit means to enter the amount on the left side of an account, to credit means to enter the amount on the right side of the account. An account has a credit balance when its credits exceed its debits. It is said to be in balance when its debits and credits are equal. With these T-accounts it is possible to formulate the rules for recording transactions using a double entry accounting system.

Type	Debit	Credit
Asset	Increases	Decreases
Liability	Decreases	Increases
Equity	Decreases	Increases
Income	Decreases	Increases
Expense	Increases	Decreases

After entries are posted to the accounts, the total of all debit balances should equal the total of credit balances. Adding all the debit balances, then adding all the credit balances, and finally

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comparing the two totals to see whether they are equal is called proving the ledger. A formal way to prove debits and credits is to prepare a trial balance. A trial balance is a list of all account names and their current balances. All the debit balances are added. All the credit balances are added. The totals are compared and should be equal. If the totals are not equal, this is your clue that an error has been made. In computerized accounting, the double entry is done for you so there is little room for error.

Cash Vs Accrual Accounting

Using the accounting period concept, accountants determine in which period the revenues and expenses of the business should be reported. To determine this period, accountants can use the (1) *cash basis of accounting* or (2) *the accrual basis for accounting*. Under the cash basis, revenues (income) and expenses are reported when the cash is received or paid. For example, sales are recorded when you have collected the funds from your customer, and the rent on your building would be expensed on your income statement when the bill is paid.

Under the accrual basis, revenue (income) is reported on an income statement in the period in which they are earned. For example, sales are reported when the service takes place. Cash may or may not have been received during this period. Under the accrual basis, expenses are reported when they incur whether or not cash is paid out. For example, a repair expense is reported as an expense when the bill was incurred not when it was paid. The accounting concept that supports reporting revenues and the related expenses in the same period is called the matching concept. Reports based on accrual provide an accurate picture of a business and should be use for the decision making process. The following flowcharts illustrate accrual vs. cash methods for sales and purchases.

Exhibit A: Sales-Accrual Method

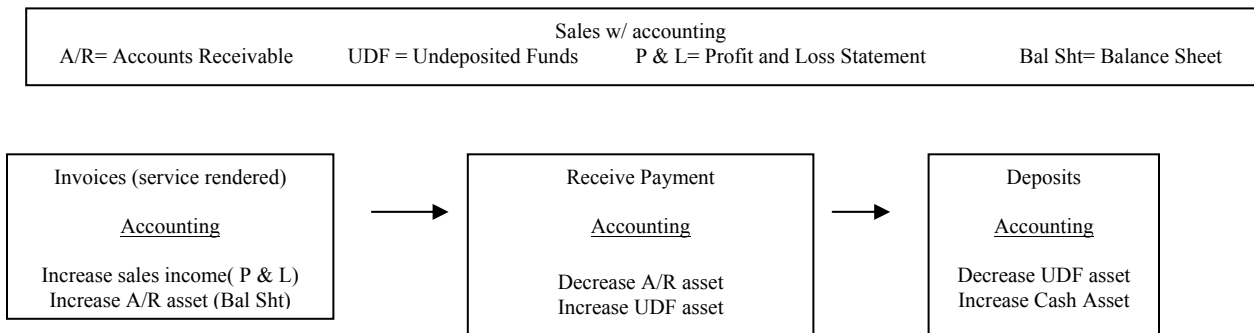


Exhibit B: Sales-Cash Method

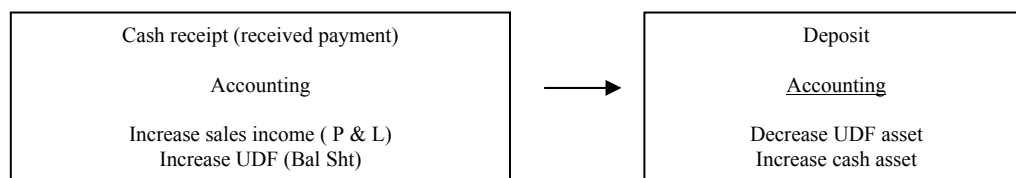
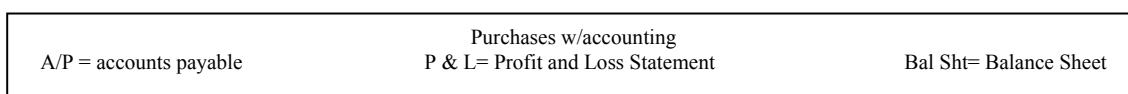


Exhibit C: Purchases-Accrual Method



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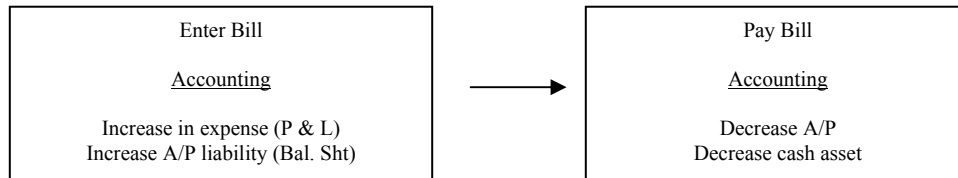
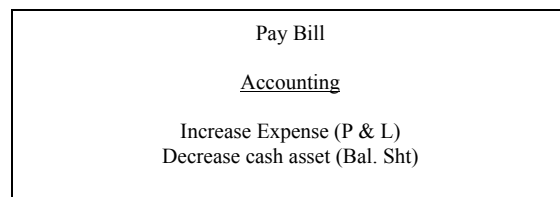


Exhibit D: Purchases-Cash Method



Many accounting packages have the ability to generate accrual and cash basis reports. A challenge for you is to look at your business using both methods. You may find it very interesting.

The topics for this advanced accounting study guide are as follows:

1. Capital sale, purchase, or trade-in
2. Depreciation Expense
3. Patronage Dividend
4. Payroll
5. Options/Hedging
6. Livestock purchases and sales
7. Commodity Credit Loans
8. Leases

Each of the following sections contains an introduction about the topic, sample problems, entry methods using increases and decreases and debits and credits, and an explanation.