

# **ACCOUNTING NOTES**

## **What is accounting?**

Is the process of recording and reporting financial transactions pertaining to a business.

Measures the results of an organization's economic activities and communicates this information to different stakeholders such as managers, creditors, investors and regulators.

## **BASIC ACCOUNTING EQUATION**

Is the principle that the company's assets are equal to the sum of its owner's equity and liabilities.

$$A = O.E + L$$

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

It shows how a change in one account affects the other accounts.

Every entry on the debit side equals entry on the credit side. This is called the double-entry bookkeeping system.

## **THE ACCOUNTING CYCLE**

Is a systematic process for recording and summarizing a company's financial transactions, in this order:

1. TRANSACTIONS: Identify and analyze transactions.

What is a transaction?

A transaction is an agreement between a willing buyer and seller to exchange goods and services for money.

Where do we record these transactions?

We record them in a flow of documents called source documents.

For every transaction that takes place in the business, there is a source document created.

## EXAMPLES OF SOURCE DOCUMENTS

Sales Invoice: Issued when a customer buys products in the business.

Receipts: Issued when a customer pays for services rendered to them (usually used in the service business).

Suppliers invoice: Received when the business pays products or services rendered to them.

Bank Statement: Is a record of all financial transactions on a bank account within a specific time period.

Good Received Note: It is also known as a "Delivery Note" is received to confirm receipt of goods.

2. JOURNAL ENTRIES: Preparing and recording transactions on the books of prime entry/ subsidiary books.

## Books of Prime Entry

This is where transactions that are made by business are recorded for the first time, before they are posted to the ledger accounts.

The following are the books of prime entry

**Sales Journal:** this journal is used to record credit sales from invoices issued.

**Purchases Journal:** This journal is used to record credit purchases from the invoices received from suppliers.

**Sales Returns Journal:** records goods purchased on credit and are being returned to the business by customers.

**Purchases Returns Journal:** Records goods purchased on credit by the business being returned to the suppliers.

**General Journal:** Is used to record non – cash items/transactions relating to adjustments entries e.g depreciation or accounting errors.

**Petty Cash Journal:** Is used to record the funds business keeps on hand to pay for small business expenses.

**Cash payment Journal:** Is used to record all transactions where a business pays for cash expenses.

**Cash receipt Journal:** Is used to record all transactions where a business receives money for cash sales or services rendered.

3. GENERAL LEDGER: Posting transactions of journals to the company's ledger accounts.

Is a set of numbered accounts known as chart of accounts a business uses to keep track of its financial transactions and to prepare financial reports.

What is an account?

- A place where business records and stores its transactions. Each transaction is recorded in a business impacts two or more entries. One debit and the other/s credit or vice versa. These entries are recorded in an account.

What is a chart of accounts?

- Is an index/list of accounts where the company files away its financial information/transactions.

**There are five (5) categories of chart of accounts**

- Assets
- Expenses
- Owner's Equity
- Income and,
- Liabilities

To start the books of a company you need to develop a chart of accounts:

EXAMPLE

<b><u>DESCRIPTION</u></b>	<b><u>TYPE OF ACCOUNT</u></b>
Motor Vehicle	Fixed Asset
Mortgage loan	Liabilities
Retained Income	Owner's Equity
Sales/Revenue	Income
Bank charges	Expenses



4. TRIAL BALANCE: Preparing the trial balance with debits and credits balances to test their equality.
- Is a report that lists the balances of a general ledger of a business at a specific date. It is used to prepare financial statements. The purpose of a Trial balance is to ensure debits equal credits in the ledger. This confirms the double-entry bookkeeping system.

**TRIAL BALANCE OF ALPHABET (PTY) LTD ON 28 FEBRUARY 2025**

ACCOUNT NAME	DEBIT (Dr)	CREDIT (Cr)
<b>Balance sheet section</b>		
Motor vehicle Bank Charges		
<b>Nominal Section</b>		
Sales Retained Income Mortgage Loan		

5. WORKSHEETS: Are used to analyze the trial balance to prepare for calculations, adjustments and financial statements.
6. ADJUSTING ENTRIES: Adjustments are made to account for accrual accounting concept.
- Adjustments are made at the end of an accounting period to ensure that income and expenses are correctly allocated to the period in which they occurred.

Below are examples of adjustments but not limit to the following:

- Depreciation: The process of reducing the value of an asset over time due to wear and tear caused by natural damages/obsolescence or passing of time e.g straight line or reducing balance method.
- Prepaid expenses: Expenses that are paid in advance (Asset).
- Accrued Income: Income earned but yet received (Asset).

- d. Accrued Expenses: Expenses incurred but not yet paid (Liability).
- e. Income received advance: Income received for goods or services not yet delivered (liability)
- f. Allowance for doubtful debts: An estimation of debtors control or accounts receivable that may not be collected or received.

7. FINANCIAL STATEMENTS: Are prepared to summarize the company's performance and position.

The written reports that show the business financial activities such as position, performance and position are called financial statements.

They are the following:

Balance Sheet

Income statement

Cash flow statement

Statement of changes in equity

Notes to the financial statement

