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Content

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Lesson 01: Introduction:

What is the Accounting?

- Accounting is a Language of Business

Another Definition:

- The systematic recording, reporting, and analysis of financial transactions of a business.
- The person in charge of accounting is known as an accountant, and this individual is typically required to follow a set of rules and regulations, such as the Generally Accepted Accounting Principles. (GAAB)
- Accounting allows a company to analyze the financial performance of the business, and look at statistics such as net profit.

Lesson 02: List of Key Accounting Terms and Definitions

If you want to start a business, get better at running your business, or get an accounting job, you need to know some essential financial accounting terms and concepts. The following is a glossary of words and phrases crucial to the accounting profession.

1. Accounting – The systematic recording, reporting, and analysis of financial transactions of a business. Accounting allows a company to analyze the financial performance of the business, and look at statistics such as net profit.

Balance Sheet

2. Balance Sheet – A quantitative summary of a company's financial condition at a specific point in time, including assets, liabilities and **net worth**. The first part of a balance sheet shows all the productive assets a company owns, and the second part shows all the financing methods (such as liabilities and **shareholders' equity**).

3. Asset – Any item of economic value owned by an individual or corporation, especially that which could be converted to cash. Examples are cash, securities, accounts receivable, inventory, office equipment, a car, and other property.

   Asset = Equity + Liability

1. Liability A liability is recorded on the balance sheet and can include accounts payable, taxes, wages, accrued expenses, and deferred revenues.

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Current liabilities are debts payable within one year, while long-term liabilities are debts payable over a longer period.

Liability = Asset – Equity

2. Shareholders' Equity – An ownership interest in a corporation in the form of common stock or preferred stock. It is calculated by taking the total assets minus total liabilities; here also called shareholder's equity or net worth or book value.

Equity = Asset – Liability

Income Statement

3. Income Statement (Profit and Loss) – An accounting of sales, expenses, and net profit for a given period. an income statement depicts what happened over a month, quarter, or year. It is based on a fundamental accounting equation (Income = Revenue – Expenses) and shows the rate at which the owners equity is changing for better or worse.

4. Revenue – The total amount of money received by the company for **goods sold** or **services** provided during a certain time period. It also includes all net sales, exchange of assets; and any other increase in owner's equity and is calculated before any expenses are subtracted.

5. Expense – Any cost of doing business resulting from revenue-generating activities.

Cash Flow Statement

6. Cash Flow Statement - A summary of the actual or anticipated incomings and outgoings of cash in a firm over an accounting period (month, quarter, year).

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It answers the questions:

1. Where the money came (will come) from?
2. Where it went (will go)?

Cash flow statements assess the amount, timing, and predictability of cashinflows and cash-outflows, and are used as the basis for budgeting and businessplanning.

7. Accounts Payable – Money which a company owes to **vendors** for **products** and **services** purchased on credit. This item appears on the company's **balance sheet** as a **current liability**, since the expectation is that the liability will be fulfilled in less than a year. When accounts payable are paid off, it represents a negative cash flow for the company.

8. Accounts Receivable – Money which is owed to a company by a **customer** for **products** and **services** provided on credit. This is often treated as a **current asset** on a **balance sheet**. A specific sale is generally only treated as an account receivable after the **customer** is sent an **invoice**.

From an accounting perspective, **assets** are divided into the following categories:

1. Current Assets (Cash, AR, Inventory.),
2. Fixed Asset (equipment, Merfesh, Car, Land, Building and so on),
3. Intangible assets (copyrights, goodwill).

Lesson 03: Computers in accounting

Uses and advantages and disadvantages of computers in accounting

Traditionally accounts were kept by the means of handwritten record. Computers have only begun to be used in some of the functions of accounting over the last fifteen years or so. As computers became cheaper, easier to use, and more powerful, more firms have decided to computerize their own accounting records. However, some firms, (albeit a declining number) still prefer to use handwritten accountings. This leads us to believe that there must be reasons for and against using computers in accounting.

What we need to consider here is how computers are used in accounting, and then we should be able to evaluate the potential uses and limitations of using computers in accounting.

How are computers used in accounting?

Most firms will make some use of a computer within accounting at some point. Some firms will have all their accounting performed by computers. What we need to understand is how the computer can be used.

Spreadsheets

A computer-generated spreadsheet is commonly used by firms when presenting their accounts. A simple spreadsheet will appear as a grid to which both numbers and text can be inserted. Each 'cell' of the spreadsheet can be used to insert data. A typical spreadsheet will appear as follows:

	2000	2001	2002	2003
	£	£	£	£
Sales	25,000	27,500	29,750	32,000
Cost of goods sold	13,000	14,500	16,900	17,500
Gross profit	12,000	13,000	12,850	14,500

One of the attractions of using a spreadsheet is that the calculations can be done by the computer. Some data, such as sales and cost of goods sold would need to be manually typed in, but then the gross profit can be automatically calculated by inserting a formulae into the relevant 'cell' which states how the profit is to be calculated, Once inserted then the formulae can apply to the whole row (or whole column) which makes the process both easier and more less likely to be inaccurate.

Obviously the example above is a fairly limited illustration of how spreadsheets can be used but for many small firms, the use of a spreadsheet is the main way in which computers are integrated into the work of the accountant.

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Lesson 04: Accounting software

There are accounting software packages then can be purchased by a firm that will perform many, if not all of the tasks that would normally be manually entered by the person responsible for the firm's accounts. These packages will be able to produce many of the accounting records that were previously produced by hand. Transactions may be entered into the computer package and many will produce the double entry records based on this one entry. Although the exact capabilities of each package will vary, it is possible that most, if not all of these packages will be able to produce invoices for purchases and sales. They calculate VAT returns, discounts and all the other areas of the accounting information system. Logically, these packages will also produce the final accounts for the business when required.

For larger firms this software can actually be tailor-made for the firm's own specific requirements. This sort of tailor made package is known as a **'bespoke'** system. These packages are normally produced by a specialist computer software firm who have experience in producing accounting packages. Technically, these packages are available for any firm, but given the expense of a bespoke system and the general low cost of a 'off the shelf' system (one that can be used by any firm), most firms will simply purchase a **general package like**:

1. **QuickBooks**

2. **DacEasy**

3. **SDS (Sahalsoftware Database System)**

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Lesson 05: Advantages of using computers within accounting

The main benefits of using computers (to any level within accounting) can be summarized as follows:

1. Increased accuracy

Computers are less likely to make errors. In fact they should not make errors at all. Things will still go wrong, but this is likely to be the fault of the person entering the data into the computer, rather than the computer itself making an error.

2. Time saving

The use of a computer should be able to speed up the whole process of keeping accounting records. This is especially likely to be the case when the firm wishes to produce the final financial statements at the end of a period. The computer will be able to extract a trial balance (if necessary at all- perhaps this won't be needed?) and produce the trading and profit and loss account as well as the balance sheet almost instantaneously, based on the data already inputted.

3. Performance analysis

Once the data has been inputted, it is possible to manipulate the existing data to produce variations on the firm's overall performance. Even a simple spreadsheet can be manipulated to consider different scenarios. For example, a firm may wish to see the effects of am increase in sales of the overall profit level. A range of forecasted accounts can be generated to see how well the firm could expect to produce in the future (this is known as sensitivity analysis).

The data can be manipulated into accounting ratios automatically, which allow managers to assess the overall performance. For example, the profits can be related to sales, to capital or to assets to see how effectively the firm is operating.

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4. Job satisfaction

The use of computers in accounting will free up time for the accountant to concentrate on more wide ranging tasks. This means that there is likely to be increased job satisfaction within he firm. Studies suggest that if workers are more satisfied or more motivated in the workplace, they are likely to be more productive in their output.

Lesson 06: Disadvantages of using computers within accounting

The use of computers does not provide a perfect solution. There are drawbacks associated with the introduction of computers.

1. Cost

Computers have fallen in price over the last ten years. Also, computers are far more powerful then earlier models. However, the cost of the computer and of any associated software packages can still present a large item of expenditure for the small firm. The purchase will not affect profits, but will affect the firm's cash flow position. The cost of training staff will also have to be factored into the equation when deciding if and what sort of accounting package to purchase.

2. Reliability

Computers are generally very reliable but problems do occur. If the computer hardware (they physical computer and other devices used in the system) or the software develops a fault, then it is likely that the whole system will not able to be used until the fault can be addressed. This could be very problematic if the fault takes time to found and corrected.

3. Training time

It may take time for operators to be trained in using any accounting package on the computer. This requires personnel to be diverted form other areas that they may have been working on. However, this problem is becoming less important as newer software packages have become increasingly 'user friendly' (easier to use to even a novice).

Lesson 07: Double entry bookkeeping

To record every business **transaction** that takes place we use an accounting system known as **double-entry bookkeeping**. It is believed that the double-entry system of bookkeeping was introduced to Europe in the early **sixteenth century** by the **monk, Luca Pacioli**, who tutored Leonardo da Vinci in mathematics. This system has been in use in most of the developed world for over 500 years and it shows no signs of declining in its popularity in recording accounting transactions.

Introduction

Double-entry bookkeeping, at first glance, appears complex and one might think that bookkeeping would need many years of practice before they can 'keep the books'. Fortunately, looks can be deceiving and almost anyone can pick up the basics of this system in a very short time. This is because the double entry system can be reduced down to some very straightforward rules.

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Double entry bookkeeping can be summarized

The whole system of double entry bookkeeping can be summarized in the following two rules:

1. All transactions have one entry in two different accounts (the double-entry bit)
2. All transactions have one debit entry (left side of account) and one credit entry (right side of account)

If you can remember these basic rules then financial accounting will be a lot more straightforward. In fact, remembering this rule can help you out of situations where you cannot remember which side one half of the transaction should be entered - just remember, if you know the debit entry then wherever the other entry is, it must be a credit entry and vice versa.

For every type of transaction, from buying new machinery to paying a supplier, there will be separate account. And each account will look roughly as follows;

Name of account					
Year	-	£	Year	-	£
Date/Month	Details	Amount	Date/Month	Details	Amount

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Let's, run through what each of these terms mean:

1. Name of account - the area that the transaction covers. There will be an account for cash, an account for every type of expense (insurance, rent and so on), an account for each type of asset (things like equipment, premises and machinery), as well as an account for each customer we sell to and each supplier we buy from (the personal accounts).
2. Date/month - the time when the transaction is undertaken
3. Details - the other account that is affected by the double entry transactions. Having the details here will help us to remember that there must always be two entries for each transaction.
4. Amount - the total monetary amount of the transaction.

For each different type of account there will be different rules governing which side of the account it is entered into. This rule will depend upon whether the amount in the account is **increasing** or **decreasing**, and also whether the account is an **Asset**, **Liability**, **Capital, Revenue or Expenses** account.

The account will always be **split** into **two** sides. It is vital that you enter the transaction not only in the correct account but also on the correct side. The two sides of each account are as follows:

Any account	
Left hand side is known as the **DEBIT SIDE**	Right hand side is known as the **CREDIT SIDE**

Debit is often abbreviated as **Dr**. and Credit is often abbreviated as **Cr**.

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Lesson 08: Five different types of accounts:

1. Asset accounts
2. Liability accounts
3. Capital accounts
4. Revenue
5. Expenses **Assets:**

Assets are any resources that are to be used in the business. Examples would include machinery, premises, stocks of goods and cash.

Liabilities:

Liabilities refer to any borrowings undertaken by the firm to a third party, for example amounts owed to suppliers, bank overdrafts, loans, etc.

Capital

Capital refers to the value of the resources put into the firm by the owner(s).

Any Asset account

Increases are entered on this side	Reductions are entered on this side

Any Liability account

Reductions are entered on this side	Increases are entered on this side

Any Capital account

Reductions are entered on this side	Increases are entered on this side

Any Revenue account

Reductions are entered on this side	Increases are entered on this side

Any Expenses account

Increases are entered on this side	Reductions are entered on this side

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Lesson 09: Accounting for purchases and sales

Therefore, we need to keep separate accounts for stock being purchased and stock being sold. In fact, we actually keep four accounts for movements in stock and these are as follows: **Increases in stock**

1. Purchases account - stocks of goods bought by the firm for resale
2. Returns inwards account - stocks previously sold that is returned by the customer due to the goods being unsuitable (e.g. they are damaged, the wrong type of goods, etc.) **Decreases in stock**

1. Sales account - stocks of goods sold to customers
2. Returns outwards account - stocks previously purchased by the firm which is returned to the original supplier

The normal double entry rules apply to all these **stock accounts**. Stock is an asset therefore, increases in stocks will always be debited to the relevant account and decreases will always be credited.

(You may also see **returns inwards** referred to as **sales returns**, and **returns outwards** as **purchases returns**)

Accounting for expenses and revenues

All firms will have expenses to pay as part of normal business activity. This will occur on a frequent basis.

Each separate expense will have its own account. Expenses do not fall into the classification of 'asset', 'liability' or 'capital', but we can still work out the rules for making entries in the expense accounts.

Any expense will require either cash or a cheque payment. Therefore, this will require a **credit entry in either the cash or the bank account**. As a result, the **debit entry must be in the expense account** - it cannot be a credit entry as it would not fit the rules of double entry bookkeeping.

Lesson 10: Accounting for drawings

Earlier in this section we saw that anything injected into the business for use in the business by the owner is known as **capital**. However, it is perfectly possible for the owner to **withdraw** resources (money or stock for example) from the business. This would be represented by a **decrease in capital.** These reductions are known as **'drawings'**.

These 'drawings' are kept in a separate **drawings account** - which is another form of capital account and follows the same double entry rules.

Balancing off accounts

At the end of each accounting period the firm will wish to balance its accounts off. An accounting period is normally one year but most firms will wish to balance off their accounts on a more frequent basis - usually every month. The more frequently a firm balances its accounts off, the less likely it is to make mistakes.

The process of balancing accounts off should not be rushed. It is, in effect, the final part of the double entry system of bookkeeping. Once accounts have been balanced off then the firm can begin to assess whether it has made a profit and if so how much profit has been generated.

The balance on each account is simply the difference in the totals of the debit side of the account and the credit side of the account. For example, if the debit side of an account added up to £190 but the credit side of the account added up to £330, then we would say that the account had a credit balance of £330 - £190 = £140.

To balance off accounts the following guidelines should be followed:

Each account must have its debit and credit columns totalled up - but don't write anything down yet.

The largest total out of the two columns will become the total for both sides and this will be written underneath each column on both sides and double underlined (double - to show that this account is finished with).

The column where the total does not add up to the total shown will need a balancing figure to make it add up. This should be entered as the 'balance to be carried down' or 'balance c/d' for short. This amount should be exactly equal to the amount needed to make the columns now both add up to the same total.

Some things to remember when balancing off accounts are:

The totals for each column should always be on the same level on the page - never at split-levels.

The balance brought down must always be on the opposite side to the balancing figure of the balance to be carried down.

The actual balance on the account is the balance brought down not the balance carried down.

An account is not really finished until the balance has been brought down to the next period.

END