

# Introduction to the Professional Bookkeeper Program

Sample Pages



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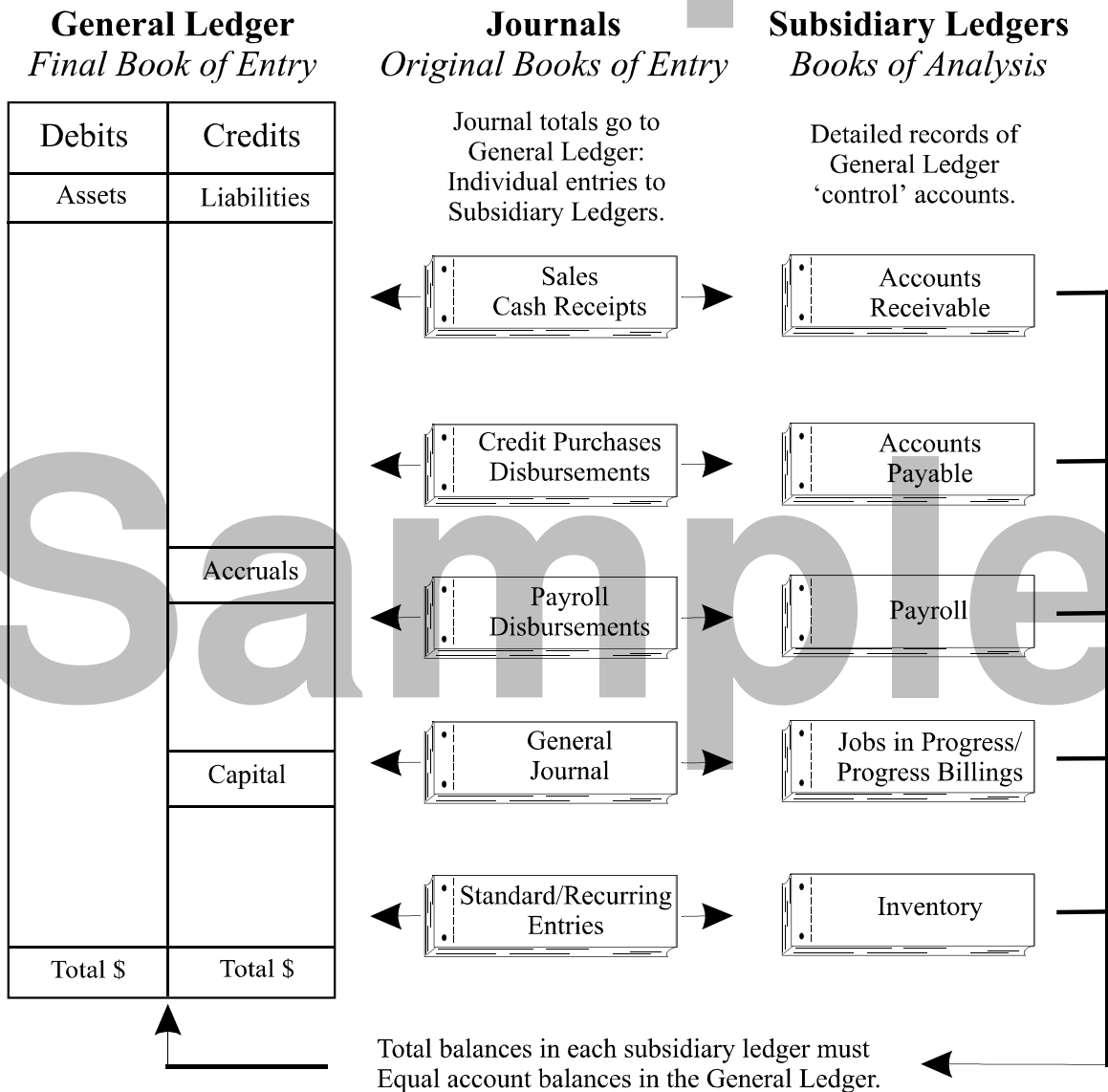
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CHAPTER ONE

# Introduction to Business Accounting

Accounting is an international skill. The books and methods used by businesses in the United States are the same as those used in Taiwan, Japan, and Belgium. Below is an illustration of a standard set of books. The purpose and use of each journal and ledger will be explained in the following pages.

Books Used in the Accounting Process



## THE GENERAL LEDGER - The Final Book of Entry

The figure on Page 1.1 shows three separate columns of simulated books. To the left is a single book called the General Ledger. No matter how large or small a business is, it needs only one General Ledger. Since it contains the totals from all the accounts in the Journals, the General Ledger is the final book of entry. It is the book from which financial statements and earnings (Profit and Loss) statements are created. It also defines the owner or stockholder's equity (ownership) in the business.

## JOURNALS - The Original Books of Entry

The books in the center column on Page 1.1 are called Journals. Sales, purchases, cash and check disbursements, bank deposits, etc. are recorded daily in these books. Anyone can be trained to copy numbers from receipts, checks, and invoices to Journals. Most often, however, small business owners and employees do not understand the complete accounting cycle, including how the Journals are related to the General and Subsidiary Ledgers.

## SUBSIDIARY LEDGERS - Books of Analysis

The books in the third column on Page 1.1 are called "Subsidiary Ledgers." They give detailed information about individual accounts recorded in the General Ledger. For example, in the General Ledger, "Customer Accounts Receivable" will have a single balance taken from the Journals, principally the Sales Journal.

The General Ledger gives no information about Bob Jones, the Boy Scouts of America, or any of the other customers who owe money to the business within the next thirty days. The General Ledger only reflects the combined total due from customers. Subsidiary Ledgers are used to give detailed information about specific accounts such as Accounts Receivable, Accounts Payable, Payroll, etc.

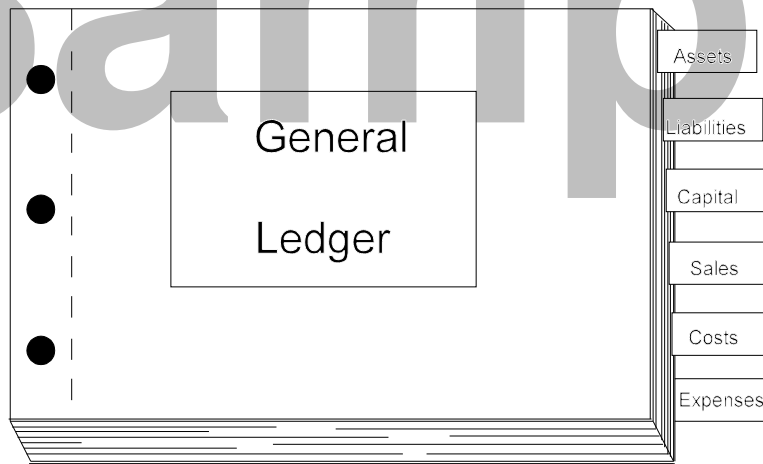
The following pages explain in detail how the General Ledger, Journals, and Subsidiary Ledgers are set up and how they work.



## THE GENERAL LEDGER

### The Final Book of Entry

The General Ledger is a perpetual record—it is never finished until a business goes out of business. At the end of each month, the bookkeeper "posts" the totals from each Journal into the corresponding accounts in the General Ledger. Each page in a General Ledger represents a separate account. Following are a sample General Ledger (with tabs separating the various types of accounts) and a sample page from Account 200 ("Bank Account—City Bank") in the General Ledger:



Bank Account - - City Bank				(Asset)	Acct. No. 200	
Date	Explanation	Post	Debit	Credit	Balance	
12/31	Beginning Balance	BB			12,436.12	
1/31		CR	15,741.15			
1/31		CD		19,602.06	8,575.21	
2/28		CR	17,537.45			
2/28		CD		13,898.11	12,214.55	
3/31		CR	14,586.54			
3/31		CD		14,645.88		
3/31		GJ		564.40	11,590.81	

The "Date" column (shown above) is used to record the date when month-end postings are made. The "Post" column is used to record the source document or journal from which the entry comes. The "Debit" column is for recording debit entries and the "Credit" column is for recording credit entries. The net balance of debits and credits is entered in the "Balance" column. If the account is classified as a debit account but has a credit balance, the balance is written in brackets (<\_\_\_\_>). In the example above, Account 200 is a debit account and has a debit

balance of 11,590.81, so no parentheses are used. This will become more clear after the discussion of debits and credits.

Following is a sample Chart of Accounts for the Balance Sheet section of the General Ledger. It shows sample assets, liabilities, accruals, and a variety of capital accounts. One duty of an accountant might be to select the general ledger accounts a business may need to use.

Current Assets (Debits)

200	Petty Cash
205	General Bank Account
206	Payroll Bank Account
210	Cash On Hand
215	Credit Card Vouchers
218	Contracts in Transit
220	Accounts Receivable
225	Employee Accounts Receivable
230	Inventory
235	Prepaid Rent
240	Prepaid Deposits
245	Notes Receivable
248	Bank Reserve Account

Property, Plant and Equipment (Debits)

250	Furniture & Fixtures
260	Machinery & Equipment
270	Leasehold Improvements
275	Vehicles
280	Buildings
285	Land

Other Assets (Debits)

291	Goodwill
292	Corporate-Owned Stocks and Bonds



Current Liabilities (Credits)

310	Accounts Payable
312	Inventory Financing (Flooring)
315	Sales Tax Payable
316	Customer Deposits
318	Payroll Payable
320	Unemployment Tax Payable
325	FICA Payable
330	Federal Withholding Payable
335	State Withholding Payable
340	Other Payroll Taxes Payable
345	Group Insurance Payable
350	Credit Union Payable

Long Term Liabilities (Credits)

355	Bank Loan #1
360	Bank Loan #2

Accruals (Credits)

Note: Although these accounts are sometimes shown in the asset section of the General Ledger, they are still "credit balance" accounts.

226	Bad Debt Allowance
251	Accum. Depreciation--Furniture
261	Accum. Depreciation--Machinery & Equipment
271	Amortization--Leasehold Improvements
276	Accum. Depreciation--Vehicles
281	Accum. Depreciation--Buildings

Capital (Credits)

380	Proprietor's Equity (Investment)
382	Partner #1 Equity
383	Partner #2 Equity
385	Common Stock (Corporation)
386	Preferred Stock (Corporation)
387	Paid in Capital
388	Retained Earnings (Corporation)
390	Drawing Account (Proprietor/Partner)
	MEMO--Annual Earnings (Balance Sheet only)

## GENERAL LEDGER "BALANCE SHEET" ACCOUNTS

The following outline describes in greater detail the four major divisions of the General Ledger Balance Sheet accounts:

### I. ASSETS — WHAT WE OWN (Debit balance accounts)

A. **Current** — Accounts that show assets with continued activity and turnover within the year.

B. **Property, Plant and Equipment** — Accounts reflecting assets owned but not intended to have a quick turnover. These items are marked down (depreciated) gradually over a number of years specified by the IRS.

C. **Other** — Assets that do not have a quick turnover and are not depreciated.

### II. LIABILITIES — WHAT WE OWE (Credit balance accounts)

A. **Current** — Liabilities with continual activity and turnover within the year.

B. **Long-Term** — Contracts payable beyond one year.

### III. ACCRUALS (Credit balance accounts)

A. **Accumulated Depreciation** — Accounts that represent markdowns in the value of fixed assets.

B. **Bad Debt Allowance** — Shows markdowns in accounts receivable.

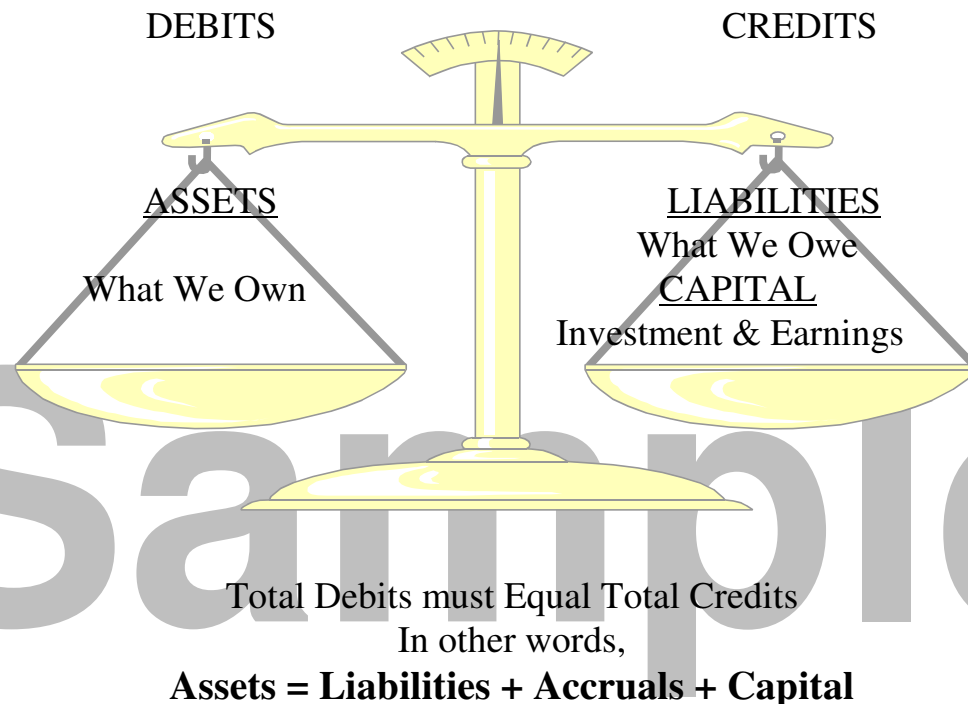
### IV. CAPITAL (Credit balance accounts)

A. **Owners' Investment/Owners' Equity** — Cash or other assets invested in a business by a proprietor or partner. During the first year of business, assets invested by owners are recorded in "Owner's Investment" account(s). At year's end, these assets are to be permanently transferred into a new account called "Owners' Equity."

- B. **Capital Stock, Retained Earnings** (in a corporation)
- C. **Draw of Proprietors/Partners** (in a single proprietorship or partnership)
- D. **MEMO: Annual Earnings** -- not a General Ledger account. "Annual Earnings" is only a Balance Sheet statistic.

A simple way to illustrate the function of the General Ledger is to describe it as a book which shows the classification and dollar value of what we own (asset accounts=debit balance) and the source from which these assets came (liabilities, accruals, investments, earnings accounts=credit balance).

The figure below illustrates the relationship between debits and credits in double-entry bookkeeping:



**Special Note** — Month-end Bank Statements

One problem that often confuses accounting students is the monthly bank statement showing your deposits as credits. The bank reports your assets as credits because that money is a liability to the bank. It owes that money back to you. Similarly, the bank reports withdrawals from your account as debits, even

though you record them as credits to your account. The bank mails out statements based on its bookkeeping records.

Since a deposit made by a company (or an individual) is an asset to that company, the bookkeeper should record it on the company's books as a debit. Withdrawals are recorded as credits. Remember: **A bank deposit increases assets and is therefore recorded as a DEBIT entry on the company's books.**

It is absolutely necessary to MEMORIZE THE DEBIT/CREDIT STATUS OF EACH CATEGORY OF ACCOUNTS in the General Ledger. Remember, an asset account is recorded as a debit account. Liabilities, depreciation, bad debts and amortization allowances, capital investments and earnings are all recorded as credit accounts.

## THE BALANCE SHEET AND THE EARNINGS STATEMENT

Every successful business relies on at least two regular reports from the General Ledger: the Balance Sheet and the Earnings (formerly Profit & Loss) Statement. These reports are compiled from the totals of the Balance Sheet accounts and the Income, Cost, and Expense accounts, respectively.

Balance Sheet accounts are those which report assets, liabilities, accruals, and capital. Earnings accounts report revenue, costs, and expenses. The profit (or loss) balance from revenue, costs, and expenses is transferred to the Capital section of the Balance Sheet. This balance is given the title "MEMO: Annual Earnings."

# Sample

**End of Sample**

# Sample



## CHAPTER TWO

# The Balance Sheet (Part I)

## Stewart's Bakery

A BALANCE SHEET is a statement that shows the assets (debits) in a business and the source from which the assets were acquired (credits). The account numbers, headings, and totals come from the General Ledger accounts. The Balance Sheet below reports January's month-end totals from the Stewart's Bakery General Ledger accounts.

### STEWART'S BAKERY JANUARY 31

#### ASSETS (Debits)

##### Current Assets

200	Petty Cash	\$ 400.00
205	Bank Account	8,575.21
215	Credit Card Vouchers	0.00
220	Accounts Receivable	19,346.16
225	Employee A/C Receivable	100.00
230	Inventory	15,039.79
240	Prepaid Deposits	200.00
245	Customer Notes Receivable	<u>5,000.00</u>
	Total Current Assets	\$48,661.16

##### Property, Plant and Equipment

250	Furniture & Fixtures	1,243.16
260	Machinery & Equipment	9,364.18
270	Leasehold Improvements	1,000.00
275	Service Vehicles	10,467.14
280	Buildings	110,000.00
285	Land	<u>15,000.00</u>
	Total PP&E	\$147,074.48

##### Other Assets

290	Goodwill	12,000.00
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#### LIABILITIES (Credits)

##### Current Liabilities

310	Accounts Payable	\$ 3,542.18
315	State Sales Tax Payable	836.40
320	Unemployment Payable	100.00
325	FICA Payroll Taxes Payable	2,389.00
330	Federal W/H Taxes Payable	2,686.80
335	State W/H Taxes Payable	435.00
345	Group Ins. Payable	<u>630.00</u>
	Total Current Liabilities	\$10,619.38

##### Long-Term Liabilities

355	Vehicle Loan	8,364.18
360	Building Mortgage	<u>92,516.88</u>
	Total Long-Term Liabilities	\$100,881.06

#### ACCRUALS (Asset Markdowns)

226	Bad Debt Allowance	500.00
251	Accumulated Depr. Furniture	110.00
261	Accumulated Depr. Machinery	1,346.00
271	Amrt. Allow. Leasehold	500.00
276	Accumulated Depr. Vehicles	5,284.00
281	Accumulated Depr. Buildings	<u>10,145.00</u>
	Total Accruals	\$17,885.00

#### CAPITAL

380	Stewart Edwards Equity	75,378.27
390	Drawing Account (Debit)	<3,000.00>
	MEMO--Earnings	<u>5,971.93</u>
	Total Capital	\$78,350.20

#### TOTAL ASSETS

\$207,735.64

#### TOTAL LIAB., ACCRLS, CAPTL

\$207,735.64

## STEWART'S BAKERY BALANCE SHEET ACCOUNTS

To simplify bookkeeping entries, accounting systems and computer programs assign every General Ledger account a number. Since all of the Asset accounts are grouped together, each can be given a number in a series. Stewart's Bakery uses the "200 series" for Asset and Asset Markdown (depreciation) accounts (see Page 2.1). Similarly, the "300 series" is used for Liability and Capital accounts. The following pages explain the use of each account in the Stewart's Bakery Balance Sheet.

### ASSETS

On Page 2.1, the accounts listed to the left are the ASSETS and represent those items owned by the business. An ASSET is recorded in a DEBIT account.

### CURRENT ASSETS

Current Assets turn over on a regular basis, usually within the year. They include cash, bank accounts, inventory, and money due from customers.

#### Acct. 200 PETTY CASH

Petty Cash is money not intended for deposit in the bank. Kept in a small metal box or a cash register, these funds are used for incidental cash purchases. When money is taken from Petty Cash, a "Petty Cash Voucher" should be filled out, explaining what the money was used for. The bill or receipt from the vendor should then be attached to the voucher and left in the box until the withdrawal from Petty Cash can be recorded on the company's books.

Amount \$ _____	No. _____
<b>Petty Cash Voucher</b>	
_____ 19 ____	
For _____	
Charge to _____	
Approved By _____	Received By _____

Petty Cash is usually reimbursed by cashing a check (withdrawing from Bank Account) and recording the transaction in a Cash Disbursement Journal. In retail stores, Petty Cash may be considered as funds left in cash registers and used for change. Alternative titles for this account may be "Register Change Fund" or "Cash in Drawer."

#### Acct. 205 BANK ACCOUNT

A company may have one, two, or several bank accounts. Stewart's Bakery has only one Bank Account. If he wished, Stewart could decide to open up a separate account exclusively for Payroll. If he were to open up bakeries all over town, he might also have an account for each bakery.

#### Acct. 215 CREDIT CARD VOUCHERS

Credit card sales not yet deposited in the bank or paid by the credit card company are recorded in Credit Card Vouchers. Credit Card Vouchers is a suspense account--its balance returns to zero once all credit card deposits are made to the bank or payments are received from the credit company.

#### Acct. 220 CUSTOMER ACCOUNTS RECEIVABLE

This account represents the combined charge accounts or monies owed by customers. Balances are considered past-due when payment has not been received within a specified time, usually 30, 60, or 90 days. At the end of each calendar month, the company mails or hand-delivers a "balance due" statement to each charge customer. When accounts are over 90 days past-due, a Bad Debt Allowance is created to reflect the loss of income.

Businesses do not normally charge interest on Accounts Receivable unless the customer fails to make payment on time. In fact, some companies actually discount sales by 1% or 2% if paid within 10 days. Another increasingly common practice is to sell goods on a "90 days same as cash" basis. While this appears to be a favor to the customer, an extra charge has usually been added into the sale price. As a result, both the cash customer and the charge customer end up paying at least 90 days' worth of interest on the sale.

#### Acct. 225 EMPLOYEE ACCOUNTS RECEIVABLE

When an employee buys inventory or services from the company without paying cash, the amount due is recorded in Employee Accounts Receivable. This account is also used to record cash advances made to employees before the payroll date. Employee Accounts Receivable are recorded separately from Customer Accounts Receivable because employees pay via payroll deduction while customers mail in payments after receiving month-end statements.

#### Acct. 230 INVENTORY

When a business purchases items for resale to the public, it records these purchases as debits to Inventory. Items which are sold are then credited from Inventory. The balance represents the wholesale value of the items still in stock.

#### Acct. 240 PREPAID DEPOSITS

Prepaid Deposit accounts show monies required by landlords and utility companies in the form of a refundable deposit. When Stewart opened his bakery, he had to pay \$200 in deposits to the telephone, electric, and gas companies before they would provide these services to his business. If Stewart closes his business at this location, he can expect \$200 back from the utility companies. If Stewart did not own the land and the building he is using for his bakery, he would probably have another account (Prepaid Rent) for security deposits made to the landlord.

#### Acct. 245 CUSTOMER NOTES RECEIVABLE

This account represents amounts due on contracts entered into between the business owner and a borrower. Customer Notes accrue interest until they are paid off. The interest received becomes an earning to the seller as it is collected or accrued.

### PROPERTY, PLANT AND EQUIPMENT

Property, Plant and Equipment has the following four characteristics: 1) They are tangible; 2) They are not held for resale; 3) They are material in value (typically greater than \$300); and, 4) They have a beneficial life of greater than one year. They include such items as furniture, buildings, vehicles, and equipment used in the business. When a business has

inventory—such as vehicles or furniture—that is being used in the business, such items should be taken out of inventory and reclassified as Property, Plant and Equipment.

A simple way to remember these four characteristics is to remember the word "TIME":

**T**angible  
**I**nventory, NOT!  
**M**ore than \$300  
**E**xpected life greater than one year



Most Property, Plant and Equipment is marked down in value over a specified number of years. However, this markdown, called depreciation, does not affect the balance of any Property, Plant and Equipment account. The balance of a Property, Plant and Equipment account changes only when an asset is bought, sold, or in some other way brought into or removed from the business. Depreciation is recorded in separate accounts called Accumulated Depreciation accounts. Depreciation is explained on Pages 2.16-20.

#### Acct. 250 FURNITURE & FIXTURES

Furniture and office equipment used in the business (not held for resale).

#### Acct. 260 MACHINERY & EQUIPMENT

Major machinery (e.g. bread mixer, press, industrial machines, ovens, etc.) owned by the business.

#### Acct. 270 LEASEHOLD IMPROVEMENTS

Improvements (not repairs) made by Stewart's Bakery to real property owned by the landlord. Examples of leasehold improvements are:

1. New walls constructed in leased buildings;
2. New carpeting installed and attached to the floor of leased buildings;
3. Construction of buildings on leased property;
4. Alterations made to leased buildings.

The cost of improvements is usually "written off" gradually over the term of

the lease. The account used for this write-off is called "Leasehold Amortization Allowance."

#### Acct. 275 SERVICE VEHICLES

Stewart's Bakery records the purchase of its delivery vans in the Property, Plant and Equipment account called Service Vehicles. As is the case with all Property, Plant and Equipment accounts, only the original Owner's Investment (purchase price plus cost of installation & Sales Tax) is recorded in this account. Depreciation and repairs are recorded in depreciation allowance and expense accounts set up specifically for these purposes.

#### Acct. 280 BUILDINGS

This account shows the cost of buildings (and improvements made to them) owned by the business. Depreciation and repairs are recorded in depreciation allowance and expense accounts set up specifically for these purposes.

#### Acct. 285 LAND

This account represents the cost (value) of land on which a business-owned building has been built. Land is not depreciated.

#### OTHER ASSETS

Other Assets represent those assets that cannot be categorized as current because of their long term nature, and don't meet, therefore, the qualifications of Property, Plant and Equipment. Examples of Other Assets are money invested by the business in goodwill, franchise fees, long-term bonds, privately held corporate stock, or other assets which are not depreciable and will not mature until after one year.

#### Acct. 290 GOODWILL

When Stewart's Bakery was purchased, the new owner, Stewart Edwards, paid \$12,000.00 more for the business than its physical assets were worth. This premium was probably the result of the good reputation of the bakery or its excellent location at the time of the sale.

## LIABILITIES

The Balance Sheet accounts shown as Liabilities represent money owed by the company. Liability accounts have credit balances and are divided into Current and Long-Term Liabilities.

### CURRENT LIABILITIES

Current Liabilities include amounts which the company owes and is expected to pay off in a period of time less than one year.

#### Acct. 310 ACCOUNTS PAYABLE

Debts which are payable in 30–90 days (without interest) are recorded in Accounts Payable. Examples of Accounts Payable are unpaid expenses and balances due on inventories received.

#### Acct. 315 STATE SALES TAX PAYABLE

By law, retail business people are required to act as sales tax collectors for the state. If sales tax is due on sold merchandise or services performed but has not been collected (e.g., if the sale is on credit, or if the business fails to charge sales tax to a cash customer), the merchant must make payment anyway. Although tax reporting is often made to the State Tax Commission on a quarterly basis, the merchant is often required to pay the sales tax every 30, 60, or 90 days.

When a company purchases items (inventory) for resale but later uses them for its own purposes, the business is required to pay a "Use Tax." This is usually levied at the same rate as Sales Tax. The Use Tax is usually included on the quarterly state sales tax report.

#### Acct. 320 UNEMPLOYMENT PAYABLE

As of 1993, the Federal Unemployment Tax Act (FUTA) requires businesses to pay FUTA tax if their employees earn combined wages of \$1,500 or more during a calendar quarter. This obligation, which Stewart records in Unemployment Payable, currently amounts to 0.8% of the first \$7,000 of each employee's annual wages. Similarly, most states charge a state unemployment tax.

Sample

**End of Sample**

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will not be equal until Earnings have been transferred from the Income Statement and added to Capital.

The Earnings MEMO on Page 2.1 indicates that Stewart's Bakery earned \$5,971.93 during January. Stewart's accountant computed this figure by subtracting January's Cost of Goods and Expenses from Sales. After December 31st of each year, the year-to-date Earnings are added to the Owner's Equity account in the General Ledger. Earnings start at zero on January 1st.

### WORKING CAPITAL AND CURRENT RATIO

Working Capital is the amount of liquid assets a business currently has at its ready disposal. Total Current Assets minus total Current Liabilities gives available Working Capital, as shown below for Stewart's Bakery (as of January 31st):

<b>STEWART'S BAKERY WORKING CAPITAL</b>	
<b>Total <u>Current</u> Assets</b>	<b>\$48,661.16</b>
<b>Less <u>Current Liabilities</u></b>	<b>- <u>\$10,619.38</u></b>
<b>Equals <u>WORKING CAPITAL</u></b>	<b>\$38,041.78</b>

Without a respectable amount of Working Capital, a business has great difficulty acquiring financing for needs such as improvements and expansion. Worse, a business that has lost its Working Capital is at high risk for failure, since its expenses (e.g. payroll, rent, utilities) continue whether or not the business is profitable. Note that Working Capital ignores Property, Plant and Equipment, Other Assets and Long-Term Liabilities.

Banks, potential buyers, and anyone else who needs to assess the financial condition of a business will also divide Current Assets by Current Liabilities to arrive at a Current Ratio. A ratio of 2:1 is considered one sign of a healthy business. Stewart's Current Ratio is 4.6:1, indicating a comfortable position.

Sample

End of Sample

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## CHAPTER THREE

# The Balance Sheet (Part II)

## City Cycle Company



Using Stewart's Bakery as an example, we explained in Chapter 2 the organization of the Balance Sheet and the purpose of some common General Ledger accounts. This chapter will use the City Cycle Company Balance Sheet to introduce several new General Ledger accounts.

### CITY CYCLE COMPANY YEAR-END BALANCE SHEET

#### ASSETS

##### Current Assets

200 Petty Cash	\$ 200.00
201 Bank Account	8,109.36
205 Contracts In Transit	1,262.18
208 Cash On Hand	0.00
210 Customer Notes	826.39
220 Customer Accts Receivable	5,072.33
224 Employee Accts Receivable	497.22
225 Factory Warranty Claims	812.43
228 Other Factory Receivables	992.89
230 Honda Cycle Inventory	11,014.08
231 Moped Inventory	4,522.26
232 Parts Inventory	13,378.54
240 Used Cycles Inventory	7,106.42
242 Miscellaneous Inventory	4,002.77
246 Sublet Repair	0.00
261 Bank Reserve Account	2,311.42
	0.00

Total Current Assets 60,108.29

##### Property, Plant and Equipment

284 Furniture & Fixtures	2,479.23
285 Service Vehicles	6,918.46
286 Leasehold Improvements	1,172.84
	0.00
	0.00
Total Property, Plant and Equipment	10,570.53

##### Other Assets

**TOTAL ASSETS** **\$70,678.82**

#### LIABILITIES

##### Current Liabilities

300 Accounts Payable	\$ 1,243.16
301 Trade-in Payoffs Payable	0.00
305 Customer Deposits	150.00
310 Flooring Payable	14,901.92
320 Interest Payable	810.23
321 Payroll Taxes FICA Payable	572.81
322 Payroll Taxes Fed Payable	1,468.21
323 Payroll Taxes State Payable	391.87
324 Sales Tax Payable	3,221.18
325 Insurance Payable	328.14
326 Licensing Payable	0.00
Total Current Liabilities	23,087.52

##### Long-Term Liabilities

330 Long-Term Loan	12,582.40
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##### ACCRUALS

384 Accum. Depr. Furn. & Fixt.	413.20
385 Accum. Depr. Service Units	830.00
386 Accum. Amort. Leaseholds	195.47
388 Allowance for Serv. Contr. Reprs	280.00
389 Bad Debt Allowance	500.00

**TOTAL LIABILITIES & ACCRUALS** **37,888.59**

##### CAPITAL

390 Common Stock (Investment)	12,000.00
395 Retained Earnings	20,790.23
Annual Earnings (Memo)	0.00

**TOTAL LIAB., ACCRLS., CAPITAL** **\$70,678.82**

Sample

End of Sample

Sample