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ACC 101 SUMMARY & PAST QUESTIONS

SUMMARY

THE BASICS

Bookkeeping is the preliminary part of accounting. It provides the reasonable bases for making financial reporting possible. Hence, bookkeeping starts from recording financial information from source documents into necessary books of account to extracting of the trial balance. In other words, the ledger and trial balance is the climax of bookkeeping. This provides the base from which the accountant extracts financial data for presentation of financial statement.

There are two main methods of bookkeeping, namely; single-entry bookkeeping and double-entry book-keeping. A single entry bookkeeping is a method of bookkeeping that relies on one sided accounting entry to maintain financial information. A double entry bookkeeping is a method of bookkeeping that relies on two sided accounting entry to maintain financial information. In whichever form it is maintained, bookkeeping plays a very significant role in an organisation. The bookkeeping section records income and liabilities of the organisation. An efficiently managed bookkeeping system in an organisation helps in determining the status of a series of key information, such as the exact cash position, the bank balance estimates, payments overdue etc.

KEY RULES AND GUIDELINES

1. Documentation

It is important to maintain paper and electronic records of all financial transactions. No matter the amount of the transaction. No amount of transaction is too small or too big to be documented.

2. Professional services

Keeping of financial record appears to be a normal routine with any kind of business endeavour. The market woman has her style of recording her financial transactions, likewise the road side mechanic or medical practitioner. It is impossible to adopt this same approach. This certainly would not work because of the different professional demands requirements. Therefore, It is important to hire professional services to handle the bookkeeping. A competent and skilled

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bookkeeper can do the job much better than the road side mechanics or medical practitioner.

3. Tracking expenses

For proper book-keeping, it is important that the authorities concerned track reimbursable expenses properly. This is especially important in case of small payments made in organisations, which must be tracked with the right procedure and recording.

4. Classify employees

All the employees, whether full-time, part-timers, freelance or independent employees should be classified appropriately for the purpose of proper bookkeeping. When these are not properly classified, it can result in misfiling when it comes to filing taxes since the rules differ on the basis of the specific category of employees.

5. Proper communication

The employees responsible for bookkeeping should be informed of all the transactions well in time. All possible receipts and relevant documents should be provided in order to avoid any errors.

6. Reconciliation

Monthly reconciliation should be done with the bank statement each month, to ensure that any possible errors or omissions are avoided. We shall discuss bank reconciliation statement in one of the subsequent units of this course material.

7. Maintain back-up

It is also important to have a complete back-up ready of all the information regarding bookkeeping. This is especially crucial in cases where the records are stored electronically which can further experience unexpected technical faults.

8. Categorization of expenses

The number and kind of expenses should be categorized in a proper manner. Both, over categorization as well as under categorization can be detrimental to the bookkeeping process.

ACCOUNTING CONCEPTS

Below are the accounting concepts:

Business Entity Concept

In accounting, we make a distinction between businesses and the owner or owners. Every business unit is treated as an entity completely different from the

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owner. All the records are kept from the viewpoint of the business rather than from that of the owner or owners.
A business is an economic unit separate and apart from the owner or owners. As such, transactions of the business and those of the owners should be accounted for and reported separately. In recording a transaction, the important question is how does it affect the business? For example, if the owner of a hospital were to take cash from the cash box for his personal use, the accounts would show that cash had been reduced by that amount even though it does not make any difference to the owner.

Going Concern Concept
Accounting assumes that the business will continue to operate for a long time in the future. The enterprise is viewed as a going concern, that is, a continuing in operation, at least in the foreseeable future. The owners have no intention to wind up or liquidate its operations.
The assumption that the business is not expected to be liquidated in the foreseeable future, in fact, establishes the basis for many of the valuations and allocations in accounting.
For example, when an hospital is established, it is assumed that that hospital will continue its operation for a long time in the future. It is the assumption which underlies the decisions of investors to commit capital to business.
The Double-Entry Concept
Every transaction involves two entries and these are both recorded in the books of account. For every debit entry, there is a corresponding credit entry. You will understand this concept better in the next unit. This will enable you to understand the double aspects and effects of a business transaction.
Accrual Concept
The accrual concept makes a distinction between the receipt of cash and the right to receive it, and the payment of cash and the legal obligation to pay it. In actual business operations, the obligation to pay and the actual movement of cash may not coincide.
This concept holds that profit is made or determined by including revenue and costs. Profit is earned not necessarily when cash is received or paid. It is not necessarily correct that cash paid or received during a particular period of time represents the time the transactions are accounted for. An example is electricity used but not yet paid for or electricity paid for but not yet used.

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Cost Concept

The resources (land, buildings, machinery, furniture etc.) that a business owns are called assets. The money values that are assigned to assets are derived from the cost concept. This concept states that an asset is worth the price paid for or cost incurred to acquire it.

Thus, assets are recorded at their original purchase price and this cost is the basis for all subsequent accounting for the assets. The assets shown on the financial statements do not necessarily indicate their present market worth or market values. The cost concept does not mean that all assets remain on the accounting records at their original cost for all time. The cost of an asset that has a long but limited life is systematically reduced during its life by a process called depreciation.

Accounting Conventions

Convention of Conservatism/ Prudence

This convention, also known as the convention of 'prudence', is often stated as 'anticipate no profit, provide for all possible losses'. This means that an accountant should follow a cautious approach. This is a convention of caution or playing safe and is adhered to while preparing the financial statements. For example, closing stock is valued at cost or market price whichever is lower.

Convention of Full Disclosure

Note that apart from legal requirements, full disclosure of all significant information should be made in the financial statements. For example, the basis of valuation of fixed assets, investments and stock should be clearly stated in the balance sheet. In other words, accounting statements should be honestly prepared.

Convention of Materiality

Whether something should be disclosed or not in the financial statements will depend on whether it is material or not, depending on the amount involved in the transaction .For example, minor expenditure of N200 for the purchase of waste basket may be treated as an expenditure of the period rather than as an asset even though the waste basket may still be in use for more than three years.

THE ACCOUNTING EQUATION AND ITS COMPONENTS

THE ACCOUNTING ENTITY

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The entity concept was introduced in the previous unit. A reporting entity is defined as "an entity for which there are users who rely on the financial statements as their major source of financial information about the entity" (ASB, 1999). Accounting for a reporting entity focuses on setting up a means of recording all accounting information in relation to that entity, as distinct from information that does not relate to the entity. The reporting entity may be a particular company, organization or business. The use of the word 'entity' emphasizes the separation between the organization and the owner(s) of the business. There is the need in accounting to decide what is, and what is not, part of the entity. Boundaries are created to show the accounting entity. The key to entity concept is realizing that these boundaries are necessary.

The accounting entity concept determines the transactions that will be recorded in the financial statements. For instance, when the managing director buys some equipment for the company's use, such a transaction is referred to as purchase made by the company. On the other hand, the expense made by the managing director in taking his family to a cinema is regarded as a personal expense. However, in some circumstance, it is difficult to determine the boundaries between business and private expenditure where an expense is incurred for both business and private purposes. It is normal to estimate the portion that is business and allocate that portion to the business entity.

ACCOUNTING EQUATION

An accounting entity may also be seen as a set of assets and liabilities. This could be seen in the statement of financial position of an entity. As an equation, this would appear as follows:

Ownership interest = Net resources of the entity

The ownership interest is called equity or owner's capital. The net resources are analysed into assets and liabilities.

An asset can defined as tangible or intangible resource that is owned by the accounting entity which is expected to generate future economic benefit. Example of assets include land, building, motor vehicles, plant and machinery, tools, office furniture, office equipment, stock (goods for resale), amount owed to the accounting entity by its customers, money in the bank and cash in hand.

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A liability can be defined as a legal obligation to transfer assets or provide services to another entity that arises from some past transaction or event. In relative simple terms, liabilities are what are owed by the company to outsiders.
Given that liabilities can be regarded as being negative in relation to assets, accounting equation can therefore be stated in the form: Assets – Liabilities = Owners' capital
Or alternatively: Assets = Owners' capital + Liabilities.
This equation is based on what is sometimes referred to as the 'dual aspect concept'. This concept proposes that every transaction has two aspects: one presented by an asset and the other a liability. This shall be explained more in the next unit.
The accounting equation is a fundamental equation and is a valuable basis from which to begin understanding the whole process of accounting. It sets out the financial position of the owners at any point in time.

ACCOUNTING PERIOD AND PROFIT REPORTING
The accounting period concept (sometimes called periodicity concept) is a means of dividing up the life of an accounting entity into discrete periods for the purpose of reporting performance for a period of time (in a statement of profit and loss) and showing its financial position at a point in time (in a statement of financial position). The period of time is usually one year and is often referred to as the accounting year, financial year or reporting period. Each accounting year of an entity's life normally ends on the anniversary of its formation, and therefore does not necessarily coincide with the calendar year. It could thus end on any day of the calendar year, but for convenience the accounting year is nearly always taken to be the end of a calendar month, and sometimes adjusted to the end of the calendar year or to the end of a particular month (e.g. for tax reasons). Some companies report on their financial position half-yearly or even quarterly. Thus, the accounting period can be less than one year.
Profit is defined in terms of potential consumption 'in a period'. Although the use of a period of a year is no more than a convention, the idea of periodic reporting is fundamental to present-day accounting. The approach adopted in accounting is an extension of the use of the entity concept. For accounting purposes, each complete period, usually of a year, is treated as a separate entity. It inherits as its opening statement of financial position the closing statement of financial position of the previous period.

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One response that follows from the needs of periodic reporting is to classify items into two types: those that will be included in the closing statement of financial position to be properly carried forward as part of the opening position of the new entity commencing the next period, and those that are properly attributable to the period just finished.

3.4 REVENUE EXPENDITURE VERSUS CAPITAL EXPENDITURE

The word 'capital' is associated with items that appear in the statement of financial position (e.g. owners' capital), whereas the word 'revenue' is associated with items that appear in the statement of profit and loss. Expenditure of the type that is to be matched against the period's revenue and is used up in the period is called revenue expenditure. Revenue expenditure will have no value at the end of the period to which it relates. Revenue expenditure is distinguished from capital expenditure – that which represents amounts which is appropriate to carry forward as part of the next year's opening statement of financial position. Capital expenditure is carried forward because it will be used over a number of periods and contributes to several periods' revenues.

Capital expenditure typically includes the cost of purchasing a non-current asset (including the costs of getting the non-current asset operational at the outset) and the cost of improvements to a non-current asset that lead to increased revenue, or sustained revenue. Expenditure on tools, which represent the long-term equipment of the business, is capital expenditure and is carried forward from one statement of financial position to another statement of financial position. Rental expenditure on building used during the year is revenue expenditure- what it provides is used up in the period. The purchase of the building, however, would be capital expenditure, as it is entirely appropriate to represent ownership being carried forward from period to period.

Allocating expenditure to the incorrect type of account has a major impact on an entity's reported performance and financial position. Revenue expenditure reduces profitability, whereas capital expenditure ends up in the statement of financial position with a portion of the expenditure being allocated to the statement of profit and loss in line with the use of the asset (the reduction in the useful economic life of the asset). To allocate capital expenditure as revenue expenditure will cause profitability to fall, vice versa. To knowingly allocate expenditure to the incorrect type of account is fraud, as users of the report will be misled and can suffer loss.

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BASIC DOCUMENTS

BUSINESS ACTIVITY

In business activity, there is the giving and taking of values. This is normally referred to as transactions. For example, where the buyer pays money or buys on credit goods from the seller. In accounting, a cash transaction is one where goods or services are paid for in cash or by cheque when they are received or delivered. A credit transaction is one where payment is made or received some time after delivery.

Credit transactions often involve trade discount. A trade discount is a discount given by one trader to another. It is usually expressed as a percentage reduction of the recommended retail price of the goods, and is deducted in arriving at the amount the buyer is charged for the goods. A large number of businesses also allow their customer cash discounts. Cash discount is the reduction in the amount that the customer has to pay, provided payment is made within a given period stipulated by the seller at the time of sale. For example, the customer will be given five percent reduction if he or she is able to pay within ten days.

DOCUMENTS INVOLVED IN CREDIT TRANSACTIONS

The main documents involved in a credit transaction are discussed below:

The invoice

The purpose of the invoice is primarily to inform the buyer how much is owed for the goods supplied by the seller. It is not a demand for payment. The information shown on an invoice typically consists of the following items:

- *The name and address of the seller;*
- *The name and address of the buyer;*
- *The invoice and delivery note number of the seller (usually the same);*
- *The date of the invoice;*
- *The address to which the goods were delivered;*
- *The buyer's order number;*
- *The quantity of goods supplied;*
- *Detailed of the goods supplied;*
- *The price per unit of each of the goods;*
- *The total value of the invoice before value added tax (VAT);*
- *When payment should be made.*

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The buyer checks the invoice against the order and delivery note (or more usually with a goods-received note prepared by the receiving department). If correct, the invoice is then entered in the buyer's books. Similarly, a copy of the invoice would have been entered in the seller's books.

The debit note

A debit note is sent by the seller if the buyer has been undercharged on the invoice. It has basically the same layout and information as the invoice except that instead of details of the goods, it shows details of the undercharge. It is recorded in the books of the seller and buyer in the same way as an invoice.

The credit note

A credit note may be sent by the seller for a number of reasons. These include:

- *The buyer has returned goods because they were not ordered, or they were the wrong type, quantity or quality, or are defective.*
- *The seller has overcharged the buyer on the invoice. This may be due to an error in the unit price or calculation.*

A credit note has basically the same layout and information as an invoice, except that instead of the details of goods, it will show the reason why it has been issued.

A credit note will be recorded in the books of the seller and buyer in a similar way to the invoice, except that the entries are the reverse. You should note that the reason why this document is called a credit note is because it informs the buyer that the account in the books of the seller is being credited. On the other hand, a debit note informs the buyer that the account in the seller's books is being debited.

The cheque

This is the most common form of payment in business because of its convenience and safety. Most cheques are crossed and therefore have to be paid into a bank account. This makes it possible to trace the cheque if it is stolen and fraudulently passed on to someone else. A crossed cheque may be paid into anyone's bank account if the payee endorses (i.e. signs) the back of the cheque. However, if the words 'account payee only' are written between the crossings it must be paid into the account of the person names on the cheque.

The information that must be shown on a cheque consists of the following;

- *The date;*
- *The signature of the drawer (i.e. payer);*

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- *The name of the drawee (i.e. the bank at which the drawer has the account);*
- *The name of the payee (i.e. who is to receive the money);*
- *The words 'Pay…' or 'Order the sum of …';*
- *The amount of money in figures and in words;*
- *The bank account number of the drawer, and the cheque and bank number are also shown on cheques.*

It is essential to write on the cheque stub (i.e. the part left with the cheque booklet after detaching the signed cheque) to whom the cheque was paid (i.e. the payee), the amount and what the payment was for. Without this information the books of account cannot be written up.

The receipt

The law requires the seller to give the buyer a receipt for goods or services that have been paid for in cash. However, there is no legal requirement to do so in the case of payments by cheque.

A receipt must contain the following information:

- *The name of the payer;*
- *The signature of the recipient;*
- *The amount of money in figures and in words;*
- *The date.*

The receipt is only recorded in the books of account when it relates to cash receipts and payments.

BOOKKEEPING VERSUS ACCOUNTING

Financial accounting as stated earlier is all about providing useful information in the financial statements to users to enable them to make economic decisions. It is all about communicating information. Recording transactions in the books of an entity is not accounting, it is bookkeeping. Accountants usually come in after the bookkeeper has finished and use the information supplied by the bookkeeper to prepare financial statements. However, to be able to account properly, accountants need to understand bookkeeping. Double-entry bookkeeping is a systematic method of recording an enterprise's transactions in a book called the general ledger or simply called the 'ledger'. Each page of the ledger is split into

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two halves: the left half is called the debit side and the right half is called the credit side.

BOOKS OF PRIME ENTRY

SALES DAY BOOK

The sale day book is a book where goods sold on credit are recorded. These goods sold are specifically bought by the buyer for resale. It is written up from copies of sales invoices and debit notes retained by the seller. The amount entered in the sales day book is after deducting trade discount (but before deducting cash discount).

At the end of each period, let say calendar month, the total of the sales day book is credited to the sales account in the general ledger and the amount of each invoice and debit note is debited to the individual credit customers' trade receivable ledger accounts in the sales ledger. Most organizations have several credit customers. Keeping separate ledger accounts for each credit customer in the general ledger and recording these in the trial balance would be cumbersome. Therefore, to reduce clutter in the general ledger and the trial balance and to serve as a control; individual credit customers are maintained in a separate ledger called the sales ledger. The total of the balances on this ledger becomes the trade receivables amount. This balance is included in the statement of financial position. An equivalent of the sales day book in the medical office is the register used to record the list of those that owe the clinic or hospital. You may observe, depending on the hospital, that as a patient is being treated, not every services rendered to the patients are paid up immediately. Sometimes, based on trust, a patient may be discharged hoping that such money would be paid on the promised date. When such situation arises, there must be a register where such transaction is recorded. This kind of record is what constitute sales day book in the business which was explained above.

SALES RETURNS DAY BOOK

This is used to record the credit notes sent to customers relating to goods they have returned or where they have been overcharged on an invoice. Note that the entry is made when a credit note has been issued, and not when the goods are returned or amount of the invoice is queried. The sales returns day book is written up from copies of the credit notes retained by the seller. The amount shown in the sales returns day book is after deducting trade discount. At the end of each period,

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the total of the sales returns day book is debited to the sales return ledger account in the general ledger and the amount of each credit note credited to the individual credit customer's trade receivable ledger accounts in the sales ledger.

PURCHASE DAY BOOK

This is used to record the purchase on credit of those goods bought specially for resale. It is written up from the invoices and debit notes received from suppliers. The amount entered in the purchases day book is after deducting any trade discount received. At the end of each period, let say calendar month, the total of the purchases day book is debited to the purchase ledger account in the general ledger and the amount of each invoice and debit note received is credited to the individual credit supplier's trade payable ledger account in the purchase ledger. Like credit customers, most organizations also have several suppliers who provide goods on credit. Keeping separate ledger accounts for each credit supplier in the general ledger and recording these in the trial balance would be cumbersome. Therefore, to reduce clutter in the general ledger and the trial and to serve as a control individual credit suppliers' ledger accounts are maintained in a separate ledger called the purchase ledger. The total of the balances on this ledger becomes the trade payable amount. This total should agree to the balance on the trade payables ledger account in the general ledger. The balance of this account is included in the statement of financial position.

PURCHASES RETURNS DAY BOOK

This is used to record the credit notes received from suppliers relating to goods returned or where there has been overcharge on an invoice. Note that the entry is made when a credit note is received and not when the goods are returned or the amount of the invoice is queried. The purchases returns day book is written up from the credit notes received from suppliers. The amount entered in the purchases returns day book is after deducting trade discount. At the end of each period, the total of the purchases returns day book is credited to the purchase returns ledger account in the general ledger and the amount of each credit note received is debited to the individual credit suppliers' trade payable ledger accounts in the purchases ledger

JOURNAL

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The journal is used to record a variety of things, most of which consist of accounting adjustments, such as the correction of errors, rather than transactions. However, the journal is also used to record transactions that are not appropriate to any other book of prime entry, the most common being the purchase sale of non-current assets on credit. These are items not specifically bought for resale but to be used in the production and distribution of those goods normally sold by the business. Non-current assets are durable goods that usually last for several years and are normally kept by the business for more than one year. Examples include land and buildings, plant and machinery, motor vehicles, furniture, fixtures and fittings, and office equipment.

Unlike the sales, purchases and returns day books, the journal has debit and credit columns. These are not a part of the double entry in the ledger. They are used to indicate what entries are going to be made in the general ledger in respect of a given transaction or adjustment. Each entry in the journal consists of the name of the ledger account that is to be debited (and the amount) and the name of the ledger account that is to be credited (and the amount). The nature of the entry must also be explained in a narrative that commonly starts with the word 'being'.

THE CASH BOOK

TWO COLUMN CASH BOOK

A two-column cash book is one in which cash received and paid are recorded in one column on each side of the cash book, and cheques received and paid are recorded in the other column on each side of the cash book. This essentially combines and replaces the ledger accounts for cash and bank.

The two-column cash book is used to record receipts and payments by cheque. It is written up from the bank paying-in book and cheque book stubs. The cash book is used instead of a bank account in the ledger. This is because there are usually a large number of transactions involving the receipt and payment of cheques, and if these were recorded in a bank account in the ledger, it would become cumbersome. Moreover, it permits a division of labour in that one person can write up the cash book while another is working on the general ledger. This also reduces the possibility of errors and provides a check on the work of the person who writes up the cash book where it is posted to the

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general ledger by someone else.
In addition to being a book of prime entry, the cash book is part of the double-entry system. Thus, debits in this book are credited to a ledger account in the general ledger and no further entries are necessary. Similarly, credits in this book are debited to an account in the ledger and no further entries are necessary.
In the format of a cash book, there will be separate column for date, particulars, folio, cash and bank.
The debit balance on the cash book represents the amount of money has in the bank and at hand. C/d and b/d represent carried down and brought down respectively.

THREE COLUMN CASH BOOK
The three-column cash book represents three accounts: cash, bank and discounts combined into one book. You would recall that the two column cash book has two money columns on the debit side and two on the credit side. Since cash discount is given as an inducement to the customers to settle their account promptly, in the three column cash book, there is the additional column for discount on both sides of the cash book. The additional column on the debit side is used to record the cash discount allowed to credit customers and the credit side is used to record the cash discount received from credit suppliers. Both of these columns require both a debit and a credit in the general ledger. Both of these additional columns are like the day books, memorandum columns in that each items entered in these columns requires both a debit and a credit in the general ledger.
Cash discount is a reduction given by the supplier of goods to a buyer if the latter pays for them within a period stipulated by the seller at the time of sale. Often in practice all goods supplied during a particular calendar month must be paid for by the end of the following calendar month if cash discount is to be obtained. You should note that cash discount is not deducted on the invoice but is calculated from the amount shown on the invoice, and deducted at the time of payment. These implies where trade discount is not offered but where trade

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discount is offered, it is computed and deducted from the invoice price before cash discount is calculated. There are two types of discount; trade discount and cash discount. Like you must have observed from the previous unit, trade discount does not appear in the book. Only cash discount will be recorded in the accounts. Apart from the entries in these two additional columns, the three-column cash book is written up in the same way as the two-column cash book. The three-column cash book is not common in practice, but is sometimes required in examination questions. The reason why the three-column cash book is not common in practice is because in most business, cash received and paid is usually recorded in a separate petty cash book instead of a cash account in the ledger.

THE PETTY CASH BOOK

THE IMPREST SYSTEM

Many firms operate their petty cash on an imprest system. At the beginning of each period, the petty cashier has a fixed amount of cash referred to as a float. At the end of each period (or the start of the next), the petty cashier is reimbursed the exact amount spent during the period, thus making the float up to its original amount. The reimbursement usually takes the form of a cheque drawn for cash. The amount of the petty cash float is determined by reference to the normal level of petty cash expenditure in each period.

The advantages of the imprest system are as follows:

1. It facilitates control of the total petty cash expenditure in each period as the petty cashier cannot spend more than the amount of the float, except by applying to the management for an increase.

2. It deters theft of cash by the petty cashier since a large cash balance cannot be accumulated by drawing cash from the bank at irregular intervals.

3. The entries in the petty cash book are kept up to date because the cash expenditure is not reimbursed until the petty cash book is written up and the total amount of expenditure for the period is known.

4. It discourages the practice of loans from petty cash since these would have to be accounted for at the end of the period, and in addition may result in insufficient cash to meet the necessary expenditure.

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THE COLUMNAR PETTY CASH BOOK

The petty cash book is used instead of a cash ledger account in the general ledger. This is because there are usually a large number of transactions in cash, and if these were recorded in a cash ledger account in the general ledger, it would become cumbersome. Like the cash book, it also permits a division of labour and facilitates improved control. In addition to being a book of prime entry, the petty cash book is part of the double-entry system. Thus, debits in this book are credited to a ledger account in the general ledger and no further entries are necessary. Similarly, credits in this book are debited to a ledger account in the general ledger and no further entries are necessary.

It is usual for a (columnar) petty cash book to have analysis columns on the credit side. Each column relates to a particular type of expenditure, such as postage, stationery or travelling expenses. These are intended to facilitate the posting of entries to general ledger. Every item of expenditure is entered in both the credit column and an appropriate analysis column. At the end of each calendar week or month, the total of each analysis column is debited to the relevant ledger account in the general ledger. Thus, instead of posting each transaction to the general ledger separately, expenditure of the same type is collected together in each analysis column and the total for the period posted to the relevant ledger account.

DOUBLE ENTRY SYSTEM OF ACCOUNTING

DOUBLE ASPECT OF TRANSACTION

Every business transaction involves two persons, one who parts with something and one who receives it. For example, in every sale, a seller and buyer are involved. The seller parts with that which is sold, and the buyer receives it. Similarly, when money is paid one person parts with it and another receives it. No matter what transaction is taken, it is always found that there are two parties, one who parts with something and one who receives it. For this reason it is said that every transaction has a double aspect; the aspect of one party parting with something and the aspect of the other receiving it.

DOUBLE EFFECT OF A TRANSACTION

Apart from the double aspect of a business transaction, what is more important still is that we should understand that every transaction has a double effect upon the finances of any single business which is a party to it.

Thus, if money is loaned to a business, an asset of a business, i.e. cash, is increased and the liabilities, i.e. the amounts owing by the business, are also increased.

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When property for use in the business is bought on credit, both an asset, e.g. buildings and the liabilities of the business are increased. When the property is paid for an asset, i.e. cash, and the liabilities of the business are both reduced. When goods or services are bought on credit, the expenditure of the business and its liabilities are both increased. When the goods and services are paid for, an asset of the business i.e. cash, and its liabilities are both reduced. Also, when goods or services are sold on credit, the income of the business is increased and an asset, i.e. debts owing by customers, is also increased.
When the customer pays for the goods or asset, i.e. debts owing by customers, is reduced. Thus, in any business every transaction in which the business is involved has a double effect upon its finances. You should note that double-entry system of accounting is designed to record thus double effect.

S/N	*Transaction*	*One Effect*	*Another Effect*
1.	*Society bought books for resale on credit*	*Its expenditure increases*	*Its debt increases*
2.	*A cooperative society pays for books bought*	*Its assets- cash decreases*	*Its debt decreases*
3.	*Cooperative society sold on credit*	*Its income increases*	*Amount owed to it increases*
4.	*Cooperative society receives money for cocoa sold*	*Its assets (cash) increases*	*Amount of sales increases*

GOLDEN RULES OF DOUBLE-ENTRY
The money value of each transaction is entered once on each side of the general ledger in different accounts. The actual process of placing the bookkeeping entry in each account is called 'posting'.
In a double-entry system of accounting one aspect or effect of a transaction is always recorded by a debit posting to a ledger account, and the other aspect or effect is always recorded by a credit posting to another ledger account.

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The essential rule of double-entry system of accounting known as Golden Rule of Double-Entry System of Accounting is that every transaction gives rise to both a debit and a credit entry, i.e. "for every debit entry, there must be a corresponding credit entry, and vice-versa, for every credit entry there must be a corresponding debit entry". Thus, the total debits and the total credits should always agree. The 'receiving' aspect of every transaction is always recorded by a debit entry in a ledger account and the "imparting" aspect is always recorded by a credit entry. Thus, when a person parts with anything which is received by the business, the account for that person in the books of the business must be credited and some other account in the books of the business must be debited. The account to be debited depends upon the nature of that which the business receives. When a person receives anything, with which the business has parted, the account of that person in the books of the business must be debited, and some other account in the books of the business must be credited. Again, the account to be credited depends upon the nature of that with which the business parts.
There are separate rules of the double entry system in respect of Personal Accounts, Real Accounts and Nominal Accounts which are discussed below:

1. Personal Accounts
As discussed earlier, these accounts record a business's dealing with persons or firms. The person receiving something is given debit and the person giving something is given credit. For example, if John sells goods to James on credit, James's Account will be debited (in John's book) as he is the receiver of goods and John's account will be credited (in James's book) as he is the giver of goods. When James makes the payment for these goods, John's Account will be debited in James's book as he is the receiver of the cash and James account will be credited in John's books as he is the giver of cash.

2. Real Accounts
These are the accounts of Assets. Assets entering the business are given debit and assets leaving the business are given credit. For example, when goods are sold for cash, cash account will be debited as cash comes in and goods accounts will be credited as goods goes out. When drugs are sold for cash, cash account will be debited while Drugs account will be credited.
So, the rule is debit what comes in and credit what goes out.
3. Nominal Accounts

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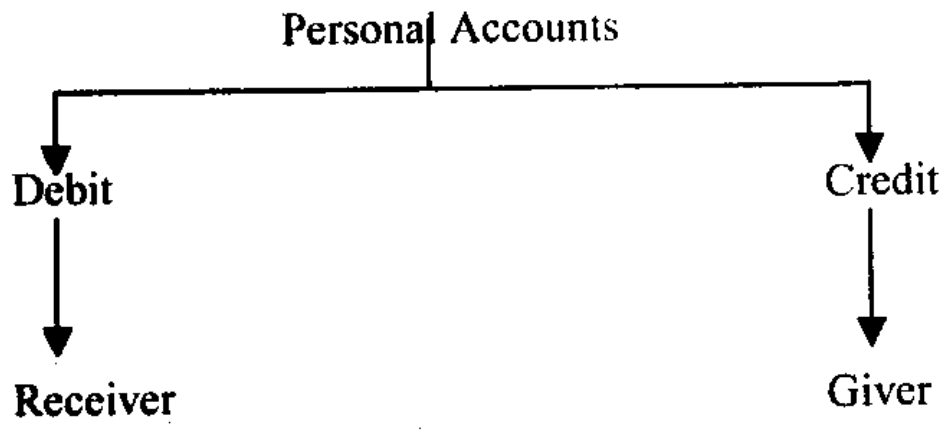
These accounts deal with expenses, incomes, profits and losses. Account of expenses and losses are debited and accounts of incomes and gains are credited. For examples, when rent is paid to the landlord, Rent account will be debited as it is an expenses and cash account (real account) will be credited as it goes out. Similarly, when commission is received, cash account will be debited as cash is received and commission account will be credited as it is an income.
Thus, the rule is: debit all expenses and losses and credit all incomes and gains.

For more explanation, the rules of double entry system of accounting are shown in the following chart:

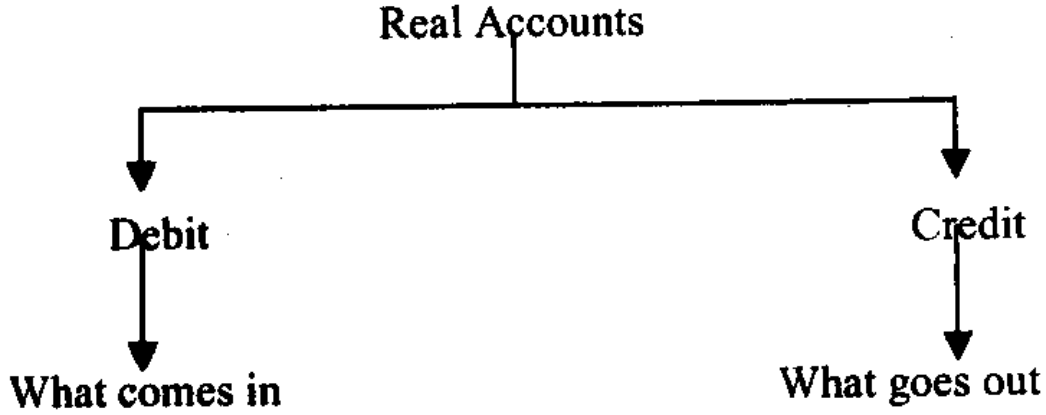
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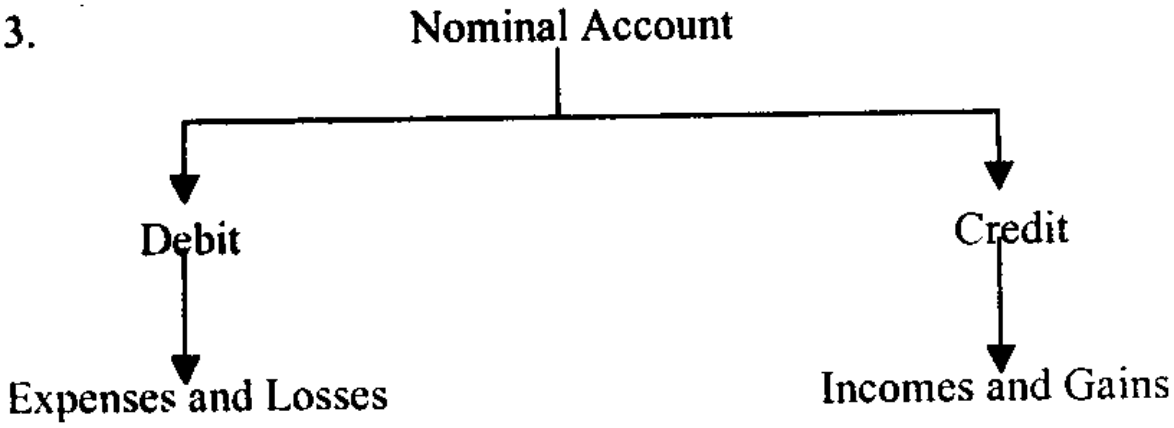
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2.



3.



THE BALANCING OF ACCOUNTS AND THE TRIAL BALANCE

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THE LEDGER

By now you must have been familiar with the word 'ledger' from previous units. It is important at this point to emphasize the use of ledger to concretize your understanding and perception of the use of ledger in book keeping. You would observe that each unit has been a build up on previous units. This is because financial reporting is actually a summary of financial information starting from posting of financial data in the source documents to the preparation and presentation of financial statements. Financial information from the basic document are entered first into the books of prime entry, from which financial information are posted to the ledger.

What then is the ledger? The ledger is the final destination of all transactions in the books of prime entries. It is the most important book of account. It can be defined as a book which contains in classified and summarized form, a permanent record of all transactions (Longe & Kazeem, 2008). The ledger is used for the double entry bookkeeping. Double-entry bookkeeping is a systematic method of recording an enterprise's transactions in a book called the general ledger or simply called the 'ledger'. Each page of the ledger is split into two halves: the left half is called the debit side and the right half is called the credit side. The ledger is divided into sections called 'accounts'. An account is a record in a double entry system that is kept for each class of item. In practice, each of these accounts is on a separate page. There is usually an 'account' for every class of expenditure, income, asset, and liability. Separate accounts are created to also record transactions into and out of the business. For example, there are typically separate accounts for wages expenses, for stationery, for electricity, for motor vehicle, loans, drawings, capital introduced by the owner and so on. There could be so much account depending on the detail required by management. Each of these 'accounts' can be traced to the financial statements. More detail is provided in the ledger than is provided in the statement of profit and loss, and in the statement of financial position (balance sheet), as too much detail would reduce the understandability of the information being presented. So, the expenses, income, assets and liabilities are usually combined in company's financial statements, to provide brief meaningful information. Indeed, many of the

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transactions that enter the ledger are summarized in other bookkeeping books beforehand to reduce the entries to the ledger.

APPLICATION OF DOUBLE ENTRY SYSTEM IN THE LEDGER

When you are faced with any transaction, ask yourself these three questions.
1. Which two accounts are affected? Mention their names.
2. What types of account are they? Classify them e.g. real, personal or nominal.
3. Which one is to be debited and which one is to be credited?

The account giving value is credited and the account receiving value is debited. In order to facilitate proper understanding of accounting, you must memorize the principle which states "credit the giver" and "debit the receiver".

NOTE:

Increase in assets is entered on the debit side of the account.
Decrease in assets is entered on the credit side of the account.
Increase in liability is entered on the credit side of the account.
Decrease in liability is entered on the debit side of the account.
Increase in income is entered on the credit side of the account.
Decrease in income is entered on the debit side of the account.
Increase in expenses is entered on the debit side of the account.
Decrease in expenses is entered on the credit side of the account.

THE BALANCING OF ACCOUNTS

It is necessary to balance each account in the ledger at the end of every accounting period. The account must be balanced off before extracting the trial balance at regular intervals during the financial year. It would be a matter of necessity to balance each account in the ledger in order to ascertain the overall position recorded in the bookkeeping system.
The procedure of balancing ledger accounts is as follows:
i. Leave one blank line under the last entry in the ledger account and draw parallel lines on the top and bottom of the next line in the amounts column on each side. When this happens it marks the end of the period. All the transactions before the totaling lines represent the period that has just ended and the area after the totaling lines represents the new period.

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ii. Add up each side of the ledger account and calculate the difference using a separate piece of paper (when you become familiar with balancing off accounts, you will no longer need to use a separate piece of paper, except perhaps for the bank account).

iii. If the amount of the debit side exceeds that on the credit side, enter the difference on the credit side immediately after the last entry on that side (in step (i) you left a blank line for this purpose). This is the closing balancing on the account. This would be describe as balance carried down (bal. c/d). Similarly where the amount on the credit side exceeds that on the debit side, the difference should be entered on the debit side immediately after the last entry on that side. Similarly, this is would be describe as balance carried down. The result is that with the entered closing balance, both sides will total exactly.

iv. Enter the total of each side of the ledger account between the parallel lines. These two figures should now be the same.

v. The difference which was used to balance the account described as balance carried down in step (iii) should be copied to the opposite side below the total of that side under the parallel lines and should be described as balance brought down (bal. b/d) representing the opening balance for the next period.

THE PURPOSE AND PREPARATION OF A TRIAL BALANCE

The trial balance is neither part of the general ledger nor is it a book of prime entry. It is a list of the balances in the general ledger at the end of an accounting period, divided between those ledger accounts with debit balances and those with credit balances. Since every transaction recorded in the ledger consists of both a debit and a credit entry, the total of the balances on each side should be the same. This is checked by entering on the trial balance the balance of each account in the ledger, and adding up each side.

The purposes of the trial balance may be summarized as follows:

1. To ascertain whether the total of the ledger accounts with debit balances equals the total of the ledger accounts with credit balances. If so, this proves that the same money value of each transaction has been entered on both sides of the general ledger. It also proves the arithmetical accuracy of the ledger accounts. However, a trial balance can agree but there may still be errors in the ledger (that would be discussed in the subsequent subunit).

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2. The trial balance is also used for the preparation of final financial statements that show the profit or loss for the period and the assets and liabilities at the end of that period.

All the ledger accounts end up in two reports in the financial statements: the statement of profit and loss and the statement of financial position (balance sheet). The ledger accounts are listed separately in the trial balance because the ledger accounts making up the statement of profit and loss are disclosed separately for user's benefits. As noted, the trial balance does not form part of the double-entry process. The trial balance is just a memorandum that is used to check the ledger accounts balance and to assist in preparing the financial statements for disclosure purposes.
The rule of the trial balance is that:
All assets must be place on the debit side of the trial balance;
All liabilities must be placed on the credit side of the trial a balance;
All income or gain must be placed on the credit side of the trial balance; and
All expenses must be placed on the debit side of the trial balance.

If a trial balance does not agree, you should adopt the following procedure which minimizes effort and time spent looking for the errors.
1. Recast the trial balance.
2. Ensure that no ledger account is omitted from the trial balance.
3. Ensure that each amount entered in the trial balance is on the correct side.
4. Ensure that the amounts entered in the trial balance are the same as those shown in the ledger accounts.
5. If the errors are still not found, it would be necessary you check all the entries in the general ledger.
ERRORS NOT DISCLOSED BY THE TRIAL BALANCE
There are some errors that cannot be shown by the trial balance. Below are the following errors.
1. Error of omission. This is when an item is completely omitted from the debit and credit sides of the books.
2. Error of commission. This occurs when an item is entered in a wrong person's account.
3. Error of original entry. This is when a wrong amount is entered on the debit and credit sides of the accounts.

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4. Error of complete reversal of entry. In this case, the item is entered on the wrong side of the account, i.e. an item that should be debited is credited and vice-versa.

5. Error of principle. This is when an item is entered in a wrong class of account.

6. Compensating errors. This occurs when errors cancelled out each other.

BANK RECONCILIATION STATEMENTS

BANK STATEMENTS AND BANK RECONCILIATION

Banks send monthly or periodical statements to their customers–individuals, hospitals, associations, corporate entities, etc. A bank statement shows details of bank's transactions (deposits, withdrawals and charges) with their customer's during a given period. At the end of the period to which the statement relates, it would indicate the balance in the account taking note of the credits (deposits) and debits (withdrawals and charges). Earlier in the introduction, we noted that it is difficult for the cashbook balance to agree with the balance on the bank statement, why?

One reason can be attributed to timing differences. For example, a cheque payment may be recorded in the cash book when it is issued. The bank only records such a cheque when it is paid by the bank, which may be several days or even weeks later (unpresented cheque).Other examples are outstanding deposits and unaccredited lodgements.

Secondly, some items may appear in the bank statement but yet to be entered in the cashbook, and these include bank charges, bank interest paid (on overdrafts) or received (on deposits), standing orders and direct debts, credit transfers (where a receipt has been paid direct into the organisations bank account), cheques returned unpaid, and unauthorised debits due to genuine mistakes or fraud. Therefore, bank reconciliation is the process of investigating the difference in both balances and attempt to agree them.

THE BANK RECONCILIATION STATEMENT

This is a statement prepared to agree the balances of both the bank statement and the cashbook. Apart from this function, the bank reconciliation statement helps to ensure that:

ü All deposits and withdrawals have been entered correctly;

ü No unauthorised debits have been made in the account; and

ü Frauds and errors are detected early and corrected.

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The reconciliation process is to verify the entries by ticking the credit side of the bank statement to the debit side of the cash book and vice versa. Any un-ticked entries in either the statement or the cashbook represent items given as examples in explaining the reasons why balances in the statement and the cashbook do not agree. The items could be treated as follow:
Unpresented Cheques have been deducted in the cashbook already but not in the bank statement.
We treat such transaction by either adding it back to cash book balance or deducting it from bank statement balance. Direct debits are either added to cash book balance or deducted from bank statement balance.
Uncredited lodgements are either added to the statement balance or deducted from cashbook balance.
Frauds and errors should be investigated and corrected.

METHODS OF BANK RECONCILIATION

There are two methods of bank reconciliation:
The first is to update the cash book by recording items in the bank statement not in it, and then, reconcile the adjusted cash book balance to the statement balance. And the second is to do straight reconciliation.

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PAST QUESTIONS

Purchase day book *is used to record goods bought on credit.*

The amount entered in the purchases day book is after deducting ***Trade discount***

At the end of each period, goods bought on credit is debited to the ***Purchase ledger account***

Given credit purchase of N90,000 from Cadbury Nigeria Ltd; N70,000 from Cable Light Ltd and cash purchase of N80,000: the purchase ledger account is debited by
Answer: N160,000

Purchase returns day book *is used to record the credit notes received from suppliers.*

Trade discount *Amount entered in the purchase returns day book is derived after deducting*

At the end of each period, the total of the purchase returns day book is _____ to the purchase returns ledger account.
*Answer****: Credited***

The purchase returns ledger account is part of the _____
Answer: General ledger

Amount of each credit note received is _____ to the trade payable accounts.
Answer: Debited

Individual trade payable ledger accounts is part of the _____

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Answer: Purchases ledger

***Journal** is used to record correction of errors rather than transactions.*

***Journal** is used to record transactions that are not appropriate to any other book of prime entry*

*The nature of the entry in the **Journal** must be explained in a narrative.*
Journal

A two-column cash** book has column for **Cash and bank

***Cash discount** is a reduction given by the supplier to the buyer for paying within stipulated time.*

Cash discount** is not deducted on the **Invoice

*Cash discount is calculated from the amount shown on the **Invoice***

*Financial information from source documents are entered first into the books of **Prime entry***

*Accounts for expenses, income, profits and losses are known as **Nominal***

*Question FBQ20 : Accounts of assets are known as **Real account.***

*Question FBQ21 : The vital rule of double-entry system of accounting is that every transaction gives rise to **Both debit and credit entry.***

*The actual process of placing the bookkeeping entry in each account is called **Posting***

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Cooperative society *sold on credit, on effect is that income increases and another effect is that* ***Amount owed to*** *it increases.*

A society paid for CDs; one effect is that cash would decrease and another effect is that ***Debt*** *would decrease.*

A society bought books for resale on credit, one effect is that expenditure would increase and another effect is that ***Debt*** *would increase.*

A petty cash book is used instead of a ***Cash ledger*** *account in the general ledger.*

Many firms operate their petty cash on ***Imprest*** *system*

The amount of petty cash float is determined by reference to the normal level of petty cash ***Expenditure***

Given balance per bank statement as N198,000, unpresented cheque of N29,000, transfer charges of N3,000, bank commission of N8,000; determine the adjusted cash book balance.
Answer: ***N169,000***

Uncredited lodgements *are either added to the statement balance or deducted from cash book balance.*

Unpresented cheques *can be deducted in the cash book but not in the bank statement.*

Bank reconciliation *is the process of investigating the difference in cash book and bank statement balances.*

Compensating errors *occur when errors cancels out each other.*

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Error of original entry *occurs when a wrong amount is entered on the debit and credit sides of the accounts.*

Question FBQ35 : When an item is entered in a wrong person's account, it is called ***Error of commission***

Which of the following is an introductory segment of accounting?
Answer: ***Bookkeeping***

In business activity, the taking and giving of values is referred to as ***Transactions***

Accounting equation is based on which of the following concepts?
Double-entry concept

Given equity as N180,000 and liabilities as N120,000; determine the assets of the business.
Answer: ***N300,000***

Given assets as N100,000 and liabilities as N40,000; determine owner's capital.
*Answer****: N60,000***

Equity *in business represents* ***Ownership interest***

The caption, 'anticipate no profit but provide for all possible losses' describes which of the conventions?
Answer: ***Prudence***

The cost of an asset is systematically reduced during its life span by a process called
Depreciation

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The assumption that a business is not expected to be liquidated in the foreseeable future relates to ***Going concern concept***

Which of the following concepts explain the occurrence of loss not necessarily when cash is received or paid?
Answer: ***Accrual concept***

Which of the following concepts distinguished an owner from the business?
Entity concept

The law requires the seller to give one of the following to the buyer for goods or services paid for in cash.
Answer: ***Receipt***

It is crucial to write the amount and what the payment is for on the cheque ***Stub*** *in order to write up the book of account.*

Which of the following must be paid into the payee's bank account?
Answer: ***Cross cheque***

Which of the following instruments will be used if a seller has overcharged the buyer on the invoice?
Answer: ***Credit note***

The layout and information of the ***debit note*** *is the same as* ***invoice*** *except it shows the details of* ***Undercharge***

Which of the following is sent if the buyer is undercharged on the invoice?
Answer: ***Debit note***

Which of the following instruments is sent to inform the buyer about the amount owed for the goods bought?

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Answer: ***Invoice***

A reduction in the amount a buyer has to pay within a given period of sale is known as ***Cash discount***

A percentage reduction in the amount a buyer is charged for goods bought is known as ***Trade discount***

Where payment is made or received after delivery is known as ***Credit transaction***

Which of the following is about providing useful information in the financial statements to enable users make economic decisions?
Answer: ***Accounting***

Which of the following is a systematic method of recording the transactions of an enterprise in a book called the ledger?
Answer: ***Double-entry bookkeeping***

The amount entered in the sales day book is after deducting ***Trade discount***

The amount entered in the sales day book is before deducting ***Cash discount***

In February 2014, Tosin Enterprise sold electric wires on credit for N50,000; electric bulbs for N20,000; and sold electric wires for cash N120,000; determine the balance of the sales day book.
Answer: ***N70,000***

Otago Enterprise bought beverages at N200,000 in March and sold beverages on credit for N150,000 and cash N120,000; what is the amount recorded in the sales day book?
Answer: ***N150,000***

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Where a customer has been overcharged by on an invoice, which of the following books is used to record the credit notes sent?
Answer: ***Sales return day book***

Given N52,000 for four bags of rice sold at 5% trade discount, N40,000 for two bags of beans, and N120,000 at 5% trade discount for eight bags of wheat; determine the balance of the sales day book.
Answer: ***N203,400***

Given trade discount of 10% on beverages bought for N350,000; determine the amount entered in the purchase day book.
Answer: ***N315,000***

Entry *is made in the* ***purchases return day book*** *when* ***Credit note*** *is received*

The sales returns day book is written up from the copies of the ***Credit notes***
There are ***Two*** *methods of bank reconciliation.*

When an item is entered in the wrong class of account, it is called ***Error of principle***

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