Financial Accounting
Chapter 2
Analyzing Transaction

I. Recording transactions -- the initial step in the accounting cycle
A. What is an account?
   1. A record keeping device used by accountants to summarize the transactions pertaining to one particular item, such as cash, accounts receivable, equipment, owner's equity, etc.
      a. Each financial statement item will have its own account
      b. Common examples are discussed on pages 44-45.

2. Concept of Account balance

3. Concept of ledger

4. Chart of Accounts

B. Recording Rules to remember
   1. Assets = Liabilities + Owner's Equity
   2. Debits = Credits
   3. This is the essence of double entry accounting

C. Journalizing the entry
   1. Some business (source) document (invoice, sales slips, cash received, check written) normally evidences need to record transactions
   2. Transactions are initially recorded in a journal
      a. In this chapter we focus on the general journal
         (1) Provides a chronological record of transactions and ties parts of the transaction together
      b. See page 58 (exhibit 4) for example of general journal entries
      c. Simple entry vs. Compound entry

II. Posting
A. Transfer information in journal entries to the general ledger
   1. Ledger -- the entire collection of accounts
      a. Each asset, liability, and owners equity item has its own ledger account and its own unique account number

B. See Exhibit 3 on page 53 for an example of the posting process.
   1. Notice use of Post Ref. Column
III. Prepare a Trial Balance
   A. A report listing all the accounts and their respective balances -- debit amounts in one column and credit amounts in the other
   B. Done to prove equality of debits and credits after entries have been posted
   C. If debits = credits is this assurance that no error exists?
   D. What if Debits do not equal Credits?
      1. Basically, review what you did in reverse order
         a. Re-add trial balance columns
         b. Find amount of difference
            (1) Divisible by 2 -- amount in wrong column?
            (2) Divisible by 9 -- transposition error?
         c. Check amounts listed in trial balance from ledger accounts
         d. Check mathematical computations in ledger accounts
         e. Review posting amounts from journals to ledger accounts
         f. Make sure debits = credits in journal entries

IV. Correcting errors.
   A. All errors detected must be corrected.
   B. In manual systems.
      1. Error discovered before posting or incorrect amount posted--correct by ruling a single line through incorrect data and writing the correct data.
      2. Incorrect account posted--prepare correcting journal entry.
   C. Computerized systems.
      1. Review software specifications--usually requires a correcting entry, cannot just "delete" incorrect entry.

V. Analysis of Financial Statements
   A. Horizontal Analysis--computing the amount and percentage change for one specific line item on the financial statements.