Accounting Systems

Accounting systems summarize a business's financial data, organize the data into useful form, and (through accountants) communicate the results to management. Management then uses the output to make a variety of business decisions.

There are 5 components to an accounting system:

1. **Source documents** -- provide the basis for making accounting entries (invoices, time cards, etc.)
2. **Input devices** -- transfer information contained in source documents to the data processing component of the accounting system. (pencils and paper, keyboards, bar code reader, scanners)
3. **Data processor** -- interprets, manipulates, and summarizes recorded information so it can be used in analyses and reports. The manual system includes the accountant, journal, ledger, and working papers.
4. **Data storage** -- paper documents or a disk or tapes
5. **Output devices** -- video screens, printers, interface between computer systems (EFT)

Many off-the-shelf accounting programs save time and minimize errors because they operate as integrated systems.

Computer **hardware** consists of the equipment needed to operate a computer system -- keyboard, central processing unit (CPU), and printer, for example.

Computer **software** consists of programs, or sets of instructions and steps that produce a desired result in a computer system.

Principles of Accounting Systems Design

In designing an accounting system, the systems designer must adhere to five general principles.

1. **cost-benefit principle** -- states that the benefits derived from the accounting system must match or exceed its cost.
2. **control principle** -- states that the accounting system must contain the safeguards necessary to protect assets and make sure the data are reliable.
3. **compatibility principle** -- states that the accounting system must be in harmony with the organization and its people.
4. **relevance principle --** requires that reports be useful, understandable, and timely for effective decision making.
5. **flexibility principle** -- states that the accounting system should be able to accommodate changes in the volume of transactions and in organizational changes within the business.

SPECIAL JOURNALS

The General Journal can be used to record any transaction. However, special purpose journals are used to increase efficiency, economy and control.

Subsidiary Accounts = contain individual accounts of a specific kind, such as customers' accounts (accounts receivable) or suppliers accounts (accounts payable). The individual account records are kept separately in a subsidiary ledger to avoid making the general ledger too bulky and to provide up-to-date records of each customer/supplier.

Controlling Accounts = Accounts in the general ledger which keeps a running total of all subsidiary accounts in a particular category (accounts receivable or accounts payable, for example).

The controlling account is updated at the end of the month. Its balance should equal the sum of all the accounts in the corresponding subsidiary account. This can be determined by creating a **schedule of accounts receivable** or **schedule of accounts payable** in which the balances in the subsidiary ledgers (accounts payable or accounts receivable) are totaled up and compared to the balance in the controlling account.

SALES JOURNAL

1. Used to record credit sales.
2. Each entry requires only one line.
3. Account names need not be written out as each entry is automatically debited to Accounts Receivable and credited to Sales
4. Explanations are not needed
5. Only total credit sales for the month, not individual sales, are posted to the sales account in the general ledger. Postings are made daily, however, to customer accounts in the accounts receivable subsidiary ledger.

Similar time-saving principles apply to the other special-purpose journals.

PURCHASES JOURNAL

1. Used to record purchases on credit.
2. A single-column purchases journal records the purchases of merchandise only. A multi-column purchases journal can accommodate the purchase of merchandise and supplies, for example.
3. Only total purchases for the month are posted to the purchases account; however, postings are made daily to creditor accounts in the accounts payable subsidiary ledger.

CASH RECEIPTS JOURNAL

1. Used to record all receipts of cash.
2. Postings to customer accounts and Other Accounts are made on a daily basis.
3. All column totals, except for Other Accounts are posted to the general ledger at the end of the month.

CASH PAYMENTS JOURNAL

1. Used to record all payments of cash.
2. Postings to creditor accounts and Other Accounts are made daily.
3. All column totals except for Other Accounts are posted to the general ledger at the end of the month.

Transactions that cannot be recorded in a special-purpose journal, such as closing entries and adjusting entries are recorded in the general journal. In cases where Accounts Receivable and Accounts Payable are affected by transactions recorded in the general journal, postings are made to both the controlling account AND the subsidiary account.

Crossfooting (or summing the journal columns and then proving that debits = credits) at the end of the month provides totals for posting and may determine errors.

A **trial balance** checks the equality of debits and credits in the general ledger after posting has been completed.

A **schedule of accounts receivable** or **schedule of accounts payable** checks to make sure that all subsidiary accounts, added together, equal the controlling account balance.

Additional information on Special Journals:

SALES JOURNAL

1. A sales journal is used to record sales on account (credit sales). This saves time and makes journalizing more efficient.
2. The source document for a sales transaction is the sales slip which records a description of the product sold, date, customer name, quantity sold, price, and whether the sale was on account or by cash.
3. Sales tax, usually collected by the business making the sale and added to the buyer's cost, will be forwarded to the government at a later date.
4. Accounts receivable subsidiary ledgers record the amounts owed by specific customers/parties. The total of all accounts receivable subsidiary ledger amounts should equal the amount listed in the general ledger accounts receivable controlling account. When posting from the sales journal, both the subsidiary ledger and the general ledger accounts receivable accounts must be updated, though at different times.
5. Frequent journal entries in the accounts receivable column of the sales journal must be posted on a regular basis to the subsidiary ledger.
6. At the end of the month, the sales and sales taxes payable columns are footed (added vertically) and a proof is made that debits equal credits. Then all three columns are posted to the general ledger. Writing the account numbers below the columns shows this has been done.

CASH RECEIPTS JOURNAL

1. A cash receipts journal is used to record all cash received by a business.
2. The source document for a cash receipt transaction is a receipt or register tape.
3. Typical cash receipts may include payment for merchandise at time of sale, payment for merchandise previously bought on account (perhaps with a bank card/credit card), sale of other assets, or a loan from the bank.
4. The rules for posting are similar to those for the sales journal except that any accounts listed in the general column must also be posted daily. In such a case, there would be a check mark at the bottom of the general column to indicate that those amounts had been posted and the total would not be posted.
5. A schedule of accounts receivable is a report listing each charge customer, the balances in each customer's account, and the total amount due from each customer. It proves that the total of all subsidiary balances equal the balance in the controlling accounts receivable account in the general ledger.

PURCHASES JOURNAL

1. A purchases journal is used to record the purchase on account of merchandise for resale.
2. The source document for transactions involving purchases is an invoice or receipt.
3. There is an accounts payable subsidiary ledger similar to the accounts receivable subsidiary ledger to keep track of individual creditor's accounts. Also, one can create a schedule of accounts payable to prove that the subsidiary ledger balances equal the controlling accounts payable balance.
4. Posting is similar to the other journals. There is only one column. Individual amounts are posted to the subsidiary accounts payable ledger and the column total is posted as a debit to purchases and a credit to accounts payable in the general ledger.

CASH PAYMENTS JOURNAL

1. A cash payments journal is used to record all payments of cash. These might include purchasing assets for cash (perhaps paying premiums on insurance—prepaid insurance asset), cash payments of expenses (utilities, for example), cash payments for items originally bought on account, shipping charges, or bank fees.
2. Follow the rules for journalizing and posting learned with the other journals.
3. Proving cash is the process of determining whether the amounts of cash recorded in a business's accounting records and in its checkbook agree.

GENERAL JOURNAL

1. The general ledger is used for purchases of items (other than merchandise) on credit, adjustments, closing entries, and correction of any errors that have already been posted.
2. When an accounts receivable or accounts payable account is journalized in the general ledger and subsidiary accounts are in use, the posting reference column must be divided in half to accommodate both the controlling account's number and the subsidiary account number.
3. Correcting entries require you to update respective accounts by increasing or decreasing them with the appropriate debit or credit.

OTHER INFORMATION:

1. In the posting reference column, S stands for the sales journal, CR for the cash receipts journal, CP for the cash payments journal, P for the purchases journal, and G for the general journal.