Accounting Cycle

Steps in the Accounting Cycle (Exhibit 2 page 140)

1. Obtain Data from Business Activities
2. Record Transactions in Accounts (journal entries)
3. Update Account Balances ("post entries in ledger")
4. Make end of period adjustments (adjusting entries)
5. Prepare Financial Statements (Balance Sheet, Income Statement, Statement of Cash Flows)
6. Close the Books (All revenue and expense balances need to be reset to zero).

Organizational Form

Organizations can take one of three different forms:

- Corporations
- Proprietorships
- Partnerships

Note that a corporation is a separate Legal Entity.
Corporations sell shares of common stock.
For a corporation, the distribution of earnings to owners is called a dividend.

Corporation:

Advantages	Disadvantages
Continuous Life	Pay separate federal income taxes
Limited Liability	Regulations
Easy transfer of ownership	Monitoring costs

Financial Accounting

- In the U.S., financial accounting rules are set by the ***Financial Accounting Standards Board (FASB)***
    - The accounting rules are called ***Generally Accepted Accounting Principles (GAAP)***
    - These are commonly accepted rules that all companies follow. Because all companies follow the same rules, investors can compare different companies and follow changes in the same company over time.
    - All companies that are publicly traded are audited by ***Certified Public Accountants*** (***CPA***s) who verify whether the financial statements conform with GAAP.

- Managerial Accounting
    - Analysis of financial information for ***internal*** users.
    - Does not have to follow GAAP or be audited by CPAs.

- Tax Accounting
    - Determines the amount of Federal Income Taxes paid.
    - Rules are determined by the ***Internal Revenue Code*** and are set by ***Congress***.

Internal Controls

- Procedures implemented by organizations to protect its assets and ensure the accuracy of its accounting information.
  - Companies need to make sure that all entries are recorded properly.
  - Companies need to safeguard their assets from theft or embezzlement.

Can you think of examples of internal controls from your own experience?

Review Problem
Ex 4-11

The following transactions apply to Rose’s Flower Shop.

a. Purchased merchandise for sale on October 1 for $3,600 to be paid by October 30.
b. Sold merchandise for $900 cash on October 3. The merchandise cost Rose’s $270.
c. Sold merchandise for $1,800 on credit on October 6. The merchandise cost Rose’s $590.
d. Ordered $2,150 of merchandise on October 7 from a supplier.
e. $400 of the merchandise purchased on October 1 spoiled on October 9 and had to be trashed, resulting in spoilage expense.
f. Paid $1,800 on October 10 to suppliers for merchandise purchased on October 1.
g. Received $1,200 on October 16 for sales of October 6.

	Account	Debit	Credit
1			