Accounting study guide chapter 3 and 4

Accrual Basis versus Cash Basis*Accrual basis: uses the adjusting process to recognize revenues when earned and expenses when incurred (matched with revenues)

*Cash basis: recognizes revenues when cash is received and records expenses when cash is paid. The revenue recognition principleRequires that revenue be recorded when earned, not before and not after. Expense recognition principleAims to record expenses in the same accounting period as the revenues that are earned as a result of those expenses. Adjusting entryrecorded to bring an asset or liability account balance to its proper amount. This entry also updates the related expense or revenue account. Prepaid expensesitems paid for in advance of receiving their benefits. Prepaid expenses, also called deferred expenses, are assets. As the assets are used, their costs become expenses. Depreciationthe process of allocating the cost of plant assets over their expected useful lives. Book valuea term used to describe the asset less its contra-asset (accumulated-depreciation). Calculate Profit MarginCalculated as net income divided by net sales revenuesSteps in closing process1) Identify accounts for closing

2) record and post the closing entries

3) prepare a post-closing trail balanceTemporary Accounts-Accumulate data related to one accounting period.

Such as revenues, expenses, owner withdrawals, and income summary. Permanent accounts-Report on activities related to one or more future accounting periods.

assets, liabilities, and owner capitalRecording Closing EntriesA) Close credit balances in revenue (and gain) accounts by debiting the accounts and crediting Income Summary. This transfers revenue balances to the credit side Income Summary.

B) Close debit balances in expense (and loss) accounts by crediting the accounts and debiting Income Summary. This transfers the expense balances to the debit side of Income Summary.

C) Close the Income Summary account to the owner's capital account.

D) Close withdrawals account by crediting the account and debiting the owner's capital accountThe ten steps repeated each accounting cycle are as follows1. Analyze transactions

2. Journalize

3. Post

4. Prepare unadjusted trial balance

5. Adjust

6. Prepare an adjusted trial balance

7. Prepare statements

8. Close

9. Prepare a post-closing trial balance.

10. Reverse (Optional)Classified Balance SheetOrganizes assets and liabilities into important subgroups that provide more information to decision makers. Current assetsAre cash and other resources that are expected to be sold, collected, or used within one year or the company's operating cycle. Long-term investmentsNotes receivable and investments in stocks and bonds are long-term assets when they are expected to be held for more than the longer of one year or the operating cycle. Plant assetsAre tangible assets that are both long-lived and used to produce or sell products and services. Intangible assetsAre long-term resources that benefit business operations, usually lack physical form, and have uncertain benefits. Current

liabilitiesObligations due to be paid or settled within one year or the operating cycle. Long term liabilitiesAre obligations not due within one year or the operating cycle. EquityIs the owner's claim on assets. Calculate Current RatioCalculation: total current assets divided by total current liabilities Tags:

- Accounting