FINANCE AT A GLANCE

Practice on using the journal

Lesson 45

In this lesson, we shall complete the analysis and journalization of the transactions presented in Lesson 44.

1 January 3, 2010

A business owner sets up his trading company by using $500,000 of his own funds as capital, and by securing a long-term debt of $400,000. No amount of the debt needs to be paid back in January.

2 January 7, 2010

Using the start-up funds, he pays cash for office equipment worth $250,000.

3 January 12, 2010

He also buys merchandise inventory worth $100,000. Of that amount, he pays off 50% upon delivery. The rest of the amount will not be due until the end of the following month.

4 January 18, 2010

He sells $35,000 of the inventory for $50,000. The buyer promises to pay in the following month.

5 January 25, 2010

He pays cash for salaries worth $5,000 and advertising expenses worth $2,500.

6 January 31, 2010

The rent for the month is $2,000, and is due for payment within the first week of the following month.

Here's the analysis of each one of the above.

Trans-action	Analysis	Account Affected	Account Type	Type of Change	Applicable Definition (See Lesson 43)	Accounting Entries
1	The business owner's money becomes the initial amount of *Capital stock*.	Capital stock	Equity	increase	5	Cr Capital stock 500,000
	The money from the bank becomes the initial amount of *Long-term debt*.	Long-term debt	Liability	increase	5	Cr Long-term debt 400,000
	The owner's money and borrowed funds go into the Company's *Cash*.	Cash	Asset	increase	1	Dr Cash 900,000

2	The purchase of equipment increases the *Fixed assets*.[1]	Fixed assets	Asset	increase	1	Dr	Fixed assets	250,000	
	The payment for that is a disbursement or decrease in *Cash*.	Cash	Asset	decrease	2	Cr	Cash		250,000
3	The purchase of merchandise is an increase in *Inventories*.	Inventories	Asset	increase	1	Dr	Inventories	100,000	
	The paid portion of the purchase is a disbursement or reduction in *Cash*.	Cash	Asset	decrease	2	Cr	Cash		50,000
	The unpaid portion becomes a debt which increases the *Accounts payables.*	Accounts payables	Liability	increase	5	Cr	Accounts payables		50,000
4	Revenue in the form of *Sales* is generated, amounting to $50,000.	Sales	Revenue		7	Cr	Sales		50,000
	Since the proceeds will be collected later, the balance of *Accounts* receivables increases.	Accounts receivables	Asset	increase	1	Dr	Accounts receivables	50,000	
	Matching this revenue is the *Cost of goods sold*, amounting to $35,000, same value	Cost of goods sold	Expense		3	Dr	Cost of goods sold	35,000	
	taken out of *Inventories*.	Inventories	Asset	decrease	1	Cr	Inventories		35,000
5	*Salaries* for the period is an expense.	Salaries	Expense		3	Dr	Salaries	5,000	
	Expenses for advertising fall under *Sales and marketing expenses*.	Sales and marketing expenses	Expense		3	Dr	Sales and marketing expenses	2,500	
	The disbursement for these expenses is reduction in *Cash*.	Cash	Asset	decrease	1	Cr	Cash		7,500
6	There is *Rent* expense for the period.	Rent	Expense		3	Dr	Rental expense	2,000	
	Because the settlement is due in the future, a liability under *Accrued liabilities* is incurred.	Accrued liabilities	Liability	increase	5	Cr	Accrued liabilities		2,000

[1] Fixed assets is the gross amount of *Net fixed assets* before adjusting for depreciation. This will be discussed later.

These above entries appear in the journal as follows:

Journal

Date	Description	Posting Ref	Debit	Credit
Jan. 3, 2010	Cash		900,000	
	Capital stock			400,000
	Long-term debt			500,000
	Initial investment and borrowing to launch the business.			
Jan. 7, 2010	Fixed assets			
	Cash		250,000	250,000
	Purchase of office equipment for cash.			
Jan. 12, 2010	Inventories		100,000	
	Cash			50,000
	Accounts payable			50,000
	Purchase of merchandise, of which half is paid with cash upfront.			
Jan. 18, 2010	Accounts receivables			
	Sales		50,000	
	Cost of goods sold			50,000
	Inventories		35,000	
	Sale of merchandise worth $35,000 for			35,000
	$50,000 on credit.			
Jan. 25, 2010	Salaries		5,000	
	Sales and marketing expenses		2,500	
	Cash			7,500
	Settlement of salaries and marketing expenses for the month.			
Jan. 31, 2010	Rent		2,000	
	Accrued liabilities			2,000
	Accrual of rent for the month.			

Before we proceed with the rest of the accounting cycle, there are concepts that need to be clarified. These will be the topics of the next few lessons.