PRINCIPLES: RULES AND DEFINITIONS FOR BOOKKEEPING

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Trieste

Principles

Rules and Definitions for Bookkeeping

BY

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Introduction

This little book was prepared to place at the disposal of the student of bookkeeping the general principles and rules needed to make intelligible the bookkeeping work.

A set of books in any business should be planned for a purpose. Knowledge of the end sought is essential to a single-minded effort to attain that end. The business man views a set of books as so much machinery for the collection and classifying of the vital facts of his business, for his guidance. The accountant plans the books so as to meet the business man's requirements. It is hoped that reference to the following pages, during the student's progress through the bookkeeping work, may enable him to take the attitude of the accountant, looking beyond the necessary details of entering, posting, and filing, to the general plan and purpose.

From the accounting standpoint, all sets of books have a likeness in certain particulars. In other particulars there is dissimilarity. We shall begin by referring to the matters which all ordinary bookkeeping systems have in common.

The first record which is similar in every business is the statement of assets and liabilities showing the net worth. Such a statement is necessary before opening a set of books, in order that the standing or financial strength may be made a matter of record.

After the business operations are under way, at regular intervals of time similar statements are made showing the changed values of the items of assets and liabilities, and the resultant changes in the net worth. These financial statements thus afford a picture of the history and progress of the business through a period of years, with a definite analysis of the condition of the business at the close of any given accounting period.

After the first statement is made, the items composing the statement are transferred to the ledger, each item under its proper heading, or account title, and each account showing the amount. During the accounting period, or interval between statements, the additions to or deductions from the several accounts of assets and liabilities are entered in the ledger, so that the accounts show, at the end of the period, the amounts to be transferred to the following statement.

The accounts that make up the net worth of the business are called **Real** accounts. The rules observed for keeping them properly are the same in any business, and may be learned once for all. On the following pages, 11 to 48, the financial statement and the real accounts are discussed in detail.

In addition to the statement of financial condition referred to, a statement of profit and loss is made at the end of the accounting period. The latter statement does not show any existing property or debts, but merely classifies the sources and amounts of incomes and expenditures. The difference between the total incomes and expenditures is either the net profit or the net loss of an accounting period. The net profit or loss agrees in amount with the increase or decrease in net worth shown by the financial statement made at beginning and end of the accounting period.

The varieties of incomes and expenditures shown in the profit and loss statement are given ledger accounts where the amounts are entered as received or expended, under the proper headings, until, at the end of the accounting period, the totals are transferred to the profit and loss statement. The accounts making up this statement are called **Nominal** accounts and represent no value except as summaries of results. The profit and loss statement and the nominal accounts are discussed on pages 48 to 70.

Every set of double entry books should be so constructed as to exhibit the elements making up the net worth in the real accounts and the elements making up the net profit or loss in the nominal accounts. The foregoing are essentials in opening and operating any double entry set of books, and if clearly in mind, comprise a sufficient basis for debit and credit.

After the ledger plan, which follows much the same order in any business, is clearly in mind, the principal, and by far the most extensive study in bookkeeping will be the methods of recording transactions and operations preparatory to transferring their amounts to the accounts. Different businesses require books in great variety of form to accommodate suitable and economical original entries. You may have the ledgers planned on the same outline for a grocery store, a printing establishment, a hotel, a coal yard, and a farm. But the details of these separate businesses are so diverse that the books of original entry will be very dissimilar in form. This is not because the general results sought differ, but because each kind of business requires first records peculiar to itself. Thus a limited cash business might find a cash book sufficient for all original entries; a limited cash and credit business might find a journal all that is needed, or more frequently a journal and a cash book; a business may have sufficient diversity of routine entries to require a dozen or more different books of original entry. Each type of business must be studied individually to determine the number and form of books of original entry suitable for its records. General suggestions about books of original entry are given on pages 126 to 152, but the more specific details necessary in each instance are to be found in the various units of work comprising the American Bookkeeping Series.

A successful bookkeeper should be able to read the ledger after he has posted it, and to keep in touch with the tendencies of the business as reflected in the accounts. He should instinctively observe failures and shortcomings in the books as a musician detects false notes in a musical scale. Suggestions about examining books are given on pages 70 to 106.

The author of this volume has used due diligence in gathering here matters of accountancy in convenient form to be consulted by the beginner in bookkeeping. Our purpose is to present these matters briefly yet with enough completeness for practical purposes.

Introductory Definitions

The pecuniary records for business purposes are prepared by bookkeepers, accountants and auditors. Though the three divisions of work indicated by these names are quite distinct in extensive and highly organized business, the bookkeeper under average conditions is also something of an accountant and auditor so far as his immediate work is concerned.

1. Accounting is the art of exhibiting the component parts of a business *organization through their expression in accounts, which are formed, continued and closed in accordance with well defined principles and rules.

An accountant arranges and prepares a bookkeeping system adapted to the needs of a given business, and derives from the system an accumulation of guiding facts, for the benefit of the business organization. He is the architect of the bookkeeping structure.

2. Bookkeeping is the art of recording business transactions and operations.

There are two principal phases of bookkeeping: (1) the preservation of a true business history of some certain *concern; (2) the classification of the items recorded in such a way as to show the receipts and disbursements of cash, and the cost and yield of the other component parts of the given concern.

A bookkeeper, as such, should know: (1) how to record all transactions that occur in a given business; (2) how to post all entries to the proper accounts; (3) how to show the condition of any account, by means of a statement; (4) how to verify his work by a trial balance; (5) how to preserve *vouchers relating to his records.

3. Auditing is the art of examining books, records, accounts and the business interests with a view to discovering the actual conditions.

An auditor is employed, ordinarily, (1) to detect fraud; (2) to prove the mechanical and mathematical accuracy of books; (3) to discover points in which the books do not conform with the principles of accountancy; (4) to exhibit the true condition of a business; (5) to make recommendations with a view to improvement.

4. Business, in the commercial sense of the term, means the various processes by which *utilities are exchanged or otherwise operated upon, with a view to profit.

A private business organization is formed for the purpose of buying or securing certain utilities, combining these into a new utility, and selling the utility thus produced. Organizations for the transaction of public business render various services to the public, and are maintained from the collection of *revenues.

Every business man should know enough about accounting, bookkeeping and auditing, to construct a useful account analysis, to make or oversee the making of good records, and to devise an adequate proof of the reliability of his own books. He should also be able, when called upon, to take charge of the *finances of a society, church, school district, township, county, city, state, or nation, or of emergency undertakings.

5. Exchanges in business are of two kinds: (1) transactions—the exchanges between persons, as in buying and selling or in collecting and paying accounts; (2) operations—the change in the conditions of values within a business; as, for example, the manufacture, collection and distribution of *commodities.

6. Entries. Every exchange involves a book entry, which is a record of the facts about the exchange and an indication of the component parts of the business affected by the exchange. The records of the facts about exchanges are called the memoranda; the names of the component parts affected by the transactions are called the account titles.

7. Books used in bookkeeping are of two general kinds: