FARM ACCOUNTING COURSE MANUAL

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This information is designed to be used as a supplement to the Farm Accounting Course, not as an instruction manual. For more information, contact your Regional Farm Economist.

Alberta
AGRICULTURE

ACCOUNTING MANUAL

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INTRODUCTION

This manual is designed to provide you with information on how to establish a record system for your farm.

WHY KEEP RECORDS

The function of record keeping and accounting is to provide financial information about a business.

- Managers need information about their business' efficiency and productivity so they can make good decisions.

- Lenders like to know the financial structure of a business and its' repayment capacity for loans.

- Accountants need good business records for tax planning and preparation of tax returns.

- By law, the government requires all businesses to keep records for tax purposes.

- Last but not least, good records help you monitor your success in achieving family goals.

So farmers need good financial records that provide them, as well as their lenders, accountants and tax officials with accurate information about the business.

RECORD SYSTEMS

A good farm record keeping system is more than just a book where you write down your income and expenses for the year. The word system means a set of things or parts forming a whole. A record keeping system, therefore, is composed of several parts, each of which contributes to the effectiveness of the whole system. The parts of a record keeping system are listed below.

1. The handling and filing of financial papers and other documents.

2. Effective use of the farm bank accounts.

3. Accurate recording of financial transactions in a record book.

4. Preparation of year end financial statements.

Used together these parts provide you with a useful accurate record system.

THE ACCOUNTING PROCESS

A quick look at the 'accounting process' shows why each of these parts is important.

1. Initial transactions are the raw material of the process; the supporting documents for these transactions (invoices, receipts) provide evidence of the completed transaction. They must be kept track of through a good system.

2. Proper use of your farm bank account through cheque writing and deposits can provide you with an almost complete record of all your transactions, - all you have to do is fill in the details.

3. The actual record keeping procedure must be done accurately and with sufficient detail to give you useful information about your business.

4. From your records are produced the final results of the accounting process, a balance sheet and an income statement. These financial statements summarize in a standard format the financial changes and the year end financial position of your business, and can be used by you, your accountant and your lender.

PAPER HANDLING AND FILING

A farm business receives a tremendous amount of paper in the form of invoices, receipts, contracts, bank statements and cancelled cheques, letters, etc.

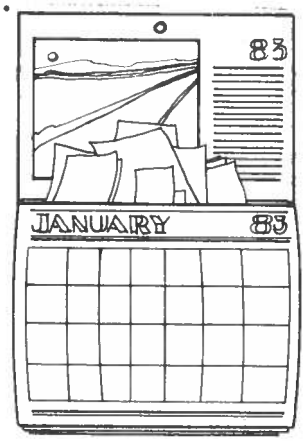
The first step to keeping good records is to have all these papers organized in a systematic manner that allows you to quickly and easily find any required information. And of course business records and supporting documents (cancelled cheques, invoices, deposit slips) have to be kept for at least five years and then can only be destroyed after permission is obtained from Revenue Canada.

This sections suggests some steps you can follow to file your financial papers.

1. Temporary File - The first step in handling papers is crucial because it seems that when documents are misplaced or lost it happens soon after they are received. Therefore, it's important that you have some sort of temporary file to hold papers until they are dealt with and then recorded and filed permanently.

   Several things can be used as a temporary file:

   - a pouch calendar can hold the mail when it arrives
   - an inexpensive briefcase can hold your chequebook and deposit book on a trip to town and then all invoices etc, that you receive can be put there
   - letter spikes
   - filing baskets



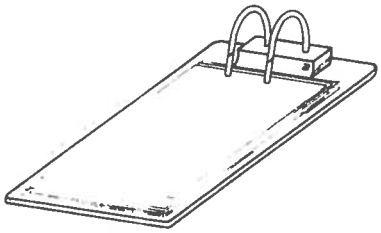
   Whatever kind of temporary file you use, it's important that you establish the habit of using it regularly so that papers and documents are kept track of.

2. Handling Papers - On a regular basis sit at your desk and sort the information in the temporary file. Pay bills, reply to letters, deposit cheques in the bank. Return any bills to be paid later to the temporary file.

3. Permanent File - File the information you need to keep in a permanent file, which can be of several types such as the two ring lock arch binding cases or file folders.

   Lock Arch Binding Case Method

   a) File invoices from expenses in one binding case. Be sure to keep bills paid by cash and bills paid by cheque This can be done by using a piece of cardboard between the cash disbursements and those paid by cheque.

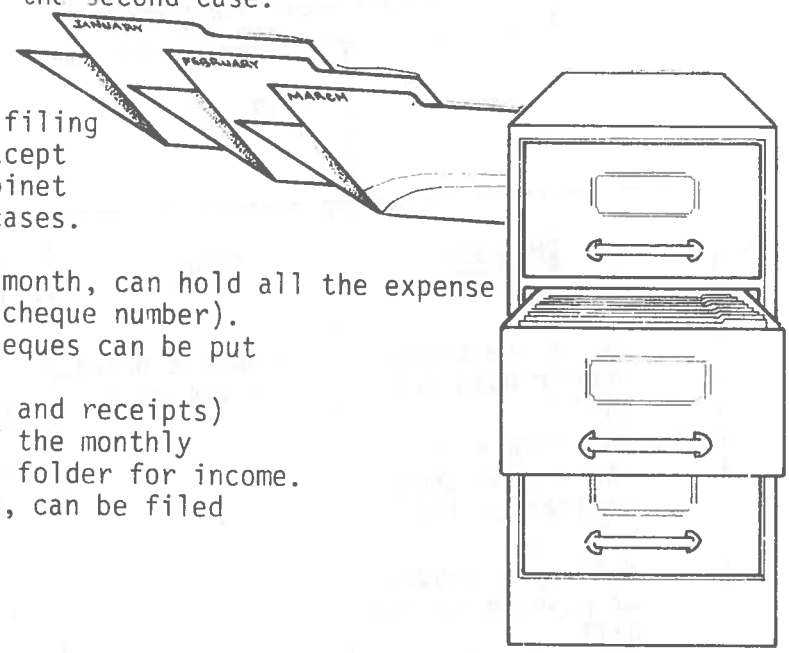


File the invoices in the order they were paid, i.e. in numerical order according to the cheque they were paid with. This makes it easier to look back through your files for a particular invoice.

b) When income is received, staple the associated cheque stubs together if more than one cheque is being deposited. These cheque stubs along with any receipts for the income should be filed in the front of the second 'Lock Arch Binding Case'. This case also can be divided into two separate sections.

c) Contracts, business letters and other important correspondence can be filed at the back of the second case.

d) Bank statements and cancelled cheques should be kept together and filed at the back of the second case.



File Folder Method

This is essentially the same filing method as the previous one except file folders and a filing cabinet are used instead of binding cases.

- Twelve file folders, labeled by month, can hold all the expense transactions (filed in order of cheque number).
- Bank statements and cancelled cheques can be put at the back of each folder.
- Income information (cheque stubs and receipts) can also be filed in the back of the monthly folder or put in a separate file folder for income.
- Contracts, business letters, etc, can be filed by subject.

It's not suggested that you file invoices by subject, since many invoices represent more than one type of expense.

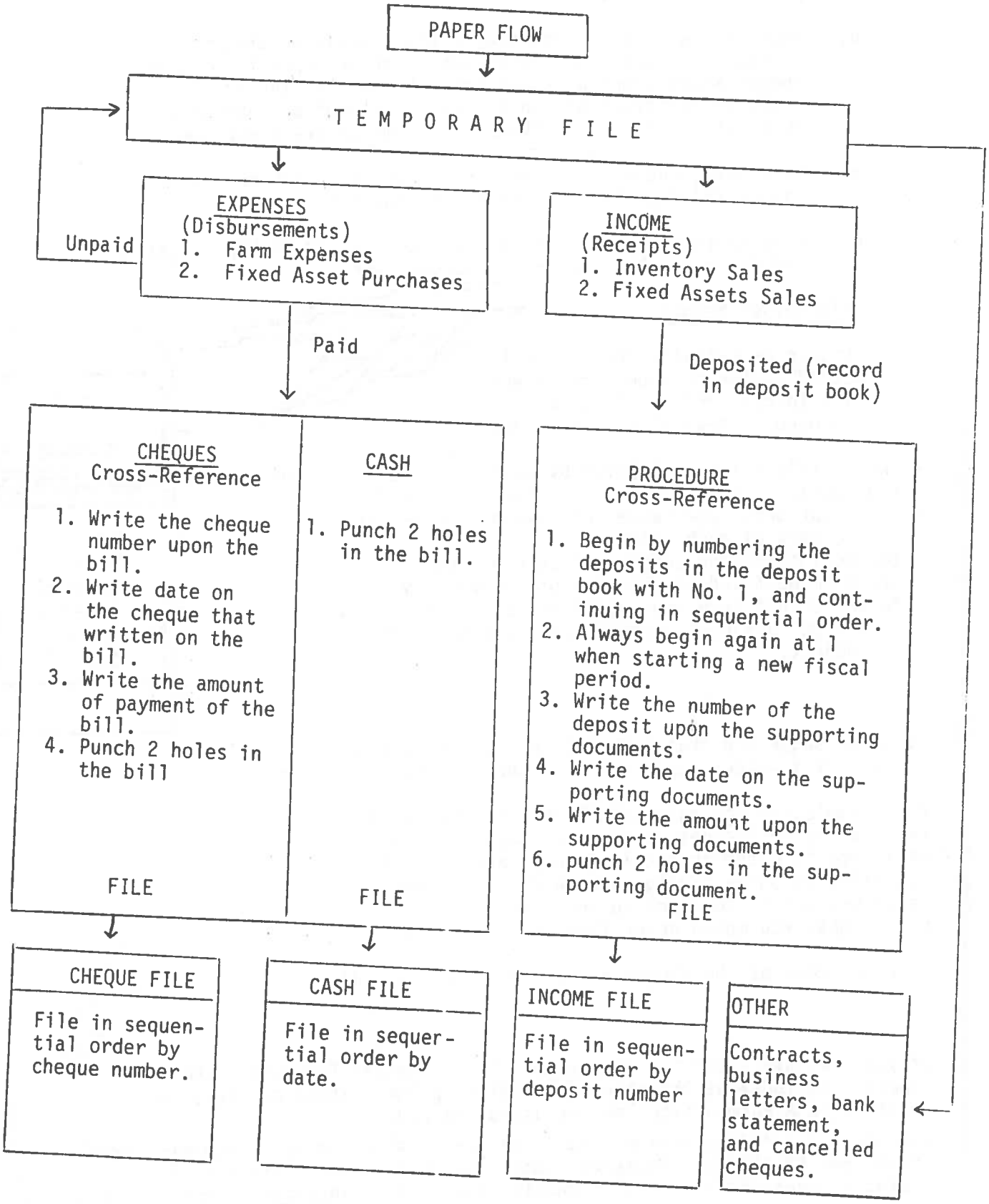
For example, if you purchased lumber for building repairs and pesticides at the same supplier, where would you file the invoice? Chances are that if you filed it under 'Building Repair' and a year later you wanted to check on the receipt for pesticides, you would never find it.

File in order of the cheque number you paid the bill with.

If you are interested in setting up a filing system for other farm papers, the index at the back of the Alberta Agriculture publication 'Setting Up A Farm Office' may be useful to you.

You may use a filing system that is different than the ones suggested here. (Yours may be better!) Whatever system you do use, make sure that it is properly organized and that it enables you to find information when you need it.

ILLUSTRATION I



USING YOUR FARM BANK ACCOUNT

Using your farm bank account correctly provides you with an excellent method for keeping track of financial transactions for record keeping. In fact your bank account may be most inexpensive bookkeeper you could ever have!

Taking advantage of what your account can do for you involves following a few rules:

1) Keep separate farm and personal bank accounts, especially if you write a lot of personal cheques.

   If you do keep separate accounts, it is important to keep them 'clean'. Use your farm account only for farm transactions and vice versa.

   There are certain advantages:
   a) It allows you to have a separate record of your farm and your personal income and expenditures.
   b) A separate farm bank account makes record keeping easier by restricting the transactions through the account to business only.
   c) Personal budgeting becomes easier. You can transfer a specific amount of money every month to your personal account, as your budget requires.

2) Pay all your farm expenses by cheque; if this isn't possible keep to a minimum the number of cash transactions. Cash transactions can be difficult to keep track of, but once you have paid a bill with a cheque the cancelled cheque remains a a permanent written record.

   Also:
   a) Use numbered cheques with your name or farm name printed on them.
   b) Record details of the payment in the cheque stub or in the cheque register. This makes record keeping much easier.
   c) Cross reference the cheque and the invoice; that is, write on the invoice the number of the cheque with which it was paid, the amount of the cheque if it was different than the amount of the invoice, and the date the cheque was written. (see Illustration I) This is very helpful if you are ever looking back through your records to check on a particular payment, especially if you made a partial payment for something.
   d) Try to use only one cheque book for the farm account. This may be difficult in a partnership situation - an alternative here would be to use the type of cheques that make a copy when the cheque is written out. These copies can be given to the person keeping the records so that that person always knows what cheques have been written.

3) Establish a system for keeping track of cash purchases. Expenses paid by cash are usually small amounts and the invoice that supports these expenses can be easily misplaced and not recorded. That leads to expenses not being claimed at tax time.

And although all business transactions should go through the farm bank account, occasions may arise when you have to pay cash or use a personal cheque for a farm expense. In this situation, keep track of the purchases paid from personal sources and reimburse yourself with a cheque from the farm bank account at the end of the month.

4) An important rule to follow is to always deposit the full amount of any income you receive in the farm bank account. If you need cash, write yourself a cheque and avoid the step of taking cash off the deposit.
   a) Keep a deposit book and use it faithfully. (See illustration)
   b) Number your deposit slips sequentially for the year.
   c) Record the details of the income you are receiving on the deposit slip - and be specific - this information can be very useful to you later.
   d) Cross reference the deposit slip and the income receipt; that is, write on the receipt the number of the deposit slip you used.
   e) Document all your deposits so that you can prove that any personal gifts or loans were not taxable farm income.

Following these rules and suggestions for your banking activities, in conjunction with using a good filing system, simplifies and streamlines the actual task of record keeping.

TYPES OF ACCOUNTS AVAILABLE

Banking instituations have a number of different types of accounts available. You should make sure that the accounts you have are the best ones for your needs.

Current Accounts, either personal or commercial, have statements prepared on a first day of the month to the last day of the month basis. This can be very useful for record keeping purposes.

Daily Interest Savings accounts allow you to earn interest on a daily basis. This is useful if you have a deposit to hold for a very short time.

True Savings Accounts have higher interest rates but it is calculated on the minimum monthly balance so withdrawals should be after the end of the month to take advantage of the higher rate.

There are a variety of personal chequing accounts available. If you write a large number of cheques consider an account that gives you unlimited cheque writing and other services for a flat monthly fee.

ILLUSTRATION II

INVOICE

IMPLEMENT DEALER LTD.
ANYWHERE, ALBERTA

October 30, 1983

QUANTITY	DESCRIPTION	AMOUNT
	Tractor Repairs Paid Nov 6/83 #53 $300.00	$648.95

CHEQUE

ANY BANK
ANYWHERE, ALBERTA

NO: 53

Date Nov 6 19 83

PAY TO
THE ORDER OF: Implement Dealer Ltd $ 300.00
THE SUM OF— three hundred 00/100 Dollars

Bill Himwell

Account No. 6074 Date Oct. 29/83

Name South Farms Ltd.

Cheques		
Tight Fisted Auction Mart (steers 39 HD)	27690	27
Joe Siesta (custom combining)	5500	00
Total cheques	33190	27

Account No. 6074 Date Oct 29/83

Credit South Farms

Deposited by B. Himwell

Cash	Dollars	Cents
____ X 1		
____ X 2		
____ X 5		
____ X 10		
____ X 20		
____ X 50		
____ X 100		
____ Coin		
Coupons		
Total Cash and Coupons		
Total Cheques	33190	27
Total Deposit	33190	27

Teller's Initials

BANK RECONCILIATION

Once every month you will receive from the bank a statement of your account. The statement shows:

1) the balance of the account at the beginning of the month
2) cheques and any other amounts deducted from the account
3) deposits and any other amounts added to the account
4) the balance of the account at the end of the month according to the records of the bank.

During a month, in addition to the cheques you have written, the bank may deduct amounts for service charges, interest charges and loan payments. These items are called debit memos. The bank may also add amounts to your account for loan advances or error corrections; these are called credit memos.

The balance appearing on your bank statement will seldom agree with the balance indicated in your records. In order to prove the accuracy of your records and the banks records it is necessary to reconcile and account for any differences between the two balances.

Several things can cause a difference between the bank statement balance and your own balance

- There may be a delay between the time you complete and record a transaction and the time the bank recognizes the transaction has taken place.
- Deposits may be made after the bank has closed its' books for the month (outstanding deposits).
- Cheques may be written but not presented to the bank and cashed before the end of the month (outstanding cheques).
- Another possibility is that either you or the bank has made errors.

It is important that you do a bank reconciliation because it forces a careful review of all transactions and it is the only way that you can ensure that the balance of your records is correct.

A bank reconciliation is a schedule indicating and explaining any differences between the banks and your business's records. It should be done monthly, after you have recorded your monthly financial transactions and when your bank statement has been returned to you.

Follow the steps suggested below:

1) Compare each cancelled cheque with the cheques entered in your record book. Indicate in your journal that the cheque was cashed.

2) List the outstanding cheques (those written by you but not cashed).

3) Compare the deposits on the bank statement with those in your records.

4) List any outstanding deposits.

5) Check that the totals on the bottom line of the reconciliation forms agree. If they don't agree, find where the mistake occurs. In the case of an error by the bank, contact them immediately as most banks will consider the statement correct if they do not hear from you within approximately 30 days.

6) File your bank statement together with the cancelled cheques and debit and credit memos.

BANK RECONCILIATION

Closing bank balance per bank statement		_____
Add: outstanding deposits	+ _____	
	+ _____	_____
Subtract: outstanding cheques	- _____	
	- _____	
	- _____	_____
Corrected balance		_____
		_____

Opening balance in records		_____
Add: deposits, credit memos shown in records	+	_____
Subtract: cheques, service charges, interest, debit memos	-	_____
Closing balance per records		_____
		_____

NOTE: The reconciled closing balance becomes next months opening balance for your records.

Following is a sample reconciliation:

BANK RECONCILIATION EXERCISE

RECORDS

	DATE	DESCRIPTION	CHEQUE OR REF. #	BANK DEPOSIT DR	BANK WITHDRAWAL CR
1	Dec 1	Surge Oil Co.	387		5,355.01
2	2	Fixit Motors	388		585.93
3	10	Get Your Books Done Right	389		43.25
4	11	Whatever Your Needs Hardware	390		56.80
5	13	Cool Threats Men's Wear	391		250.00
6	14	Grow 'Em Quick Feed Mills	392		9,855.37
7	18	Happy Valley Vet Services	393		185.00
8	20	Aloof Accounting Services	394		1,500.00
9	21	Happy Valley County	395		2,335.21
10	23	Keep 'Em Underfinanced Development Corporation	396		12,353.78
11	24	Cash	397		800.00
O/S 12	29	Easy Money Auction Mart	398		26,783.31
O/S 13	29	Keep Your Plants Happy Fertilizers	399		10,000.00
O/S 14	31	Kill 'Em Dead Chemicals	400		4,558.62
15	10	Grow 'Em Quick Feed Mills	D18	7,880.53	
O/S 16	31	Tight Fisted Auction Mart	D19	25,001.99	
17	31	Interest	IN		1,533.46
18	31	Service Charge	SC		2.24
19	23	Operating Loan	LN	15,000.00	
				47,882.52	76,197.98

BANK RECONCILIATION EXERCISE

BANK STATEMENT
THE OURTOWN BANK, ALBERTA

STATEMENT OF ACCOUNT

Account No.	Page
Dec.31.1982 period ended	Encs.

BALANCE FORWARD FROM PREVIOUS STATEMENT → 12,367.05

DESCRIPTION		CHEQUES	DEPOSITS	DATE M	DATE D	'-' if overdrawn BALANCE
Cheque	387	5,355.01		12	03	7,012.04
Cheque	388	585.93		12	09	6,426.11
Deposit			7,880.53	12	11	14,306.64
Cheque	390	56.80		12	14	14,249.84
Cheque	389	43.25		12	15	14,206.59
Cheque	392	9,855.37		12	17	4,351.22
Cheque	391	250.00		12	18	4,101.22
Cheque	393	185.00		12	19	3,916.22
Cheque	394	1,500.00		12	21	2,416.22
Cheque	395	2,335.21		12	22	81.01
Loan			15,000.00	12	23	15,081.01
Cheque	396	12,353.78		12	24	2,727.23
Cheque	397	800.00		12	24	1,927.23
Interest		1,533.46		12	31	393.77
Service Charge		2.24		12	31	391.53

NO. DEBITS	TOTAL AMOUNT DEBIT	NO. CREDITS	TOTAL AMOUNT CREDIT	BALANCE
13	34,856.05	2	22,880.53	391.53

BANK RECONCILIATION

Closing bank balance per bank statement			391.53
Add: outstanding deposits	+ 25,001.99	(D19)	
	+		25,393.52
Subtract: outstanding cheques	- 26,783.31	(398)	
	- 10,000.00	(399)	
	- 4,558.62	(400)	41,341.93
Corrected balance			(15,948.41)

Opening balance in records		12,367.05
Add: deposits, credit memos show in records	+	47,882.52
		60,249.57
Subtract: cheques, service charges, interest, debit memos	-	76,197.98
Closing balance per records		(15,948.41)

NOTE: The reconciled closing balance becomes next months opening balance for your records.

BANK RECONCILIATION
(When books aren't done on a monthly basis)

This method is used when accounting records aren't being entered on a monthly basis. Accounting for outstanding cheques and deposits makes little sense since all the transactions occurred so far in the past. You should however account for outstanding cheques and deposits at the end of the fiscal period. A brief outline of the technique follows:

1) Using the bank statement and cancelled cheques, the transactions shown on the bank statement should be entered in your journal.

2) A bank reconciliation could then be done to indicate and explain any differences between the bank's and the business's records.

   An example of this follows.

	Date 1982	Description	Chq. or Ref.#	Bank Deposit DR.	Bank Withdrawal CR.
1	Sept. 20	Urban Cowboy	355		150 00
2	18	Honest Ernie's	352		27 79
3	18	Disco Shoes	353		25 00
4	20	Slim Jim's Hardware	354		6 70
5	28	Eaton's	357		125 00
6	29	Whatever You Need Hardware	356		389 00
7	Oct. 1	Jim Overworked	358		1 055 12
8	5	Night Life Fashions	360		165 00
9	1	Receiver General	359		242 16
10	6	Cure All Vet Services	361		35 00
11	12	A.G.T.	364		24 26
12	10	Honest Ernie's	362		107 04
13	10	Fran's Hair Styles	363		85 00
14	12	Fit Rite Bearings	365		45 00
15	16	Specific Machining	366		55 00
16	19	Smooth Ride Tires	367		70 00
17	23	Handling Charge	HC		50
18	23	Service Charge	SC		2 74
19	Sept. 20	Alberta Wheat Pool	D13	4 266 38	
20	28	Slim Slick's Auction Mart	D14	2 837 47	
21	Oct. 5	Grow Em' Quick Feed Mills	D15	6 903 07	
22					
23					
24				14 006 92	2 610 31
25					
26					
27					
28					

BANK RECONCILIATION
AS AT OCTOBER 23, 1982

CLOSING BANK BALANCE PER BANK STATEMENT	17,317.46
OPENING BANK BALANCE	5,920.35
ADD: DEPOSITS, CREDIT MEMOS, ETC.	14,006.92
	19,927.77
DEDUCT: CHEQUES WRITTEN, SERVICE CHARGES, INTEREST, DEBIT MEMOS, ETC.	2,610.31
CLOSING BANK BALANCE PER BOOKS	17,317.46

Close doesn't count when doing a bank reconciliation. It has to balance exactly or the process isn't worth doing.

Errors can offset each other to make two large recording mistakes look like one small error. For instance, a difference of $1.00 when doing a bank reconciliation could be caused by:

1) not recording a loan principal payment of $10,000 (not that serious - the lender records the payment and it's not a lost tax expense)
2) not recording income of $9999. (this is more serious - this amount was not included for income tax purposes).

If Revenue Canada audited these records they would find the income. There would be a tax penalty and interest to be paid on the taxes owing - an expensive mistake.

Conveivably, equal errors could offset each other - this would be very rare however.

Errors can occur in several ways:

1) The person recording transactions in the record book has done so incorrectly.

2) The bank has made an error.

If your bank reconciliation doesn't balance, don't despair. There are some ways to find your mistake.

FINDING MISTAKES

Step 1

Find exactly how much the difference is between the two amounts you are comparing.

Step 2

Depending on the amount of the difference try one of the following:

A. If the difference is evenly divisible by 9 (ie. 18,36,54, etc.),
- you may have transposed numbers that is written 91 instead of 19.
- you may have added or dropped 0's - that is written 30 instead of 300.

B. If the difference can be evenly divided by 2,
- you may have 'debited' instead of 'credited'. Divide the number by 2 and look for that exact figure. ie. If you are out by 12.00, look for a 6.00 entry that may have been 'debited' instead of 'credited', or vis versa.

C. If the difference is the exact amount of a recording entry you may have forgotten to record that transaction fully. ie. If you are out by $7.31 and you have an entry for that amount, make sure you have both 'debited' and 'credited' that entry.

D. You may have added or subtracted incorrectly. Check your calculations.

DOUBLE ENTRY ACCOUNTING

This manual illustrates the use of double entry bookkeeping methods for farm financial records. Single entry books, like most of the standard farm record keeping books available, can not be considered adequate for keeping precise accurate records of the complex and numerous financial transactions which a farm business must record. There are several reasons for this:

1) The ground rule of accounting is that all accounting information must be consistent among businesses so that the users of the information; accountants, lenders and tax officials; can understand it. Double entry record keeping is the accepted 'industry standard' in the accounting world.

2) Your accounting records should be totally accurate. This can only be achieved using a double entry method because it provides a built in check system so that errors can be located and corrected. Also, your books can be reconciled to your bank statement, providing a second check system to remove any possible error.

3) Single entry records are not designed to be used in producing a comprehensive set of financial statements (balance sheet and income statement) at year end. Double entry accounting records can be used to generate these important statements.

Using a blank accounting journal and entering your own column headings for income and expenses gives you a record book designed for your own accounting needs.

Accounting is called the language of business; and it's important that you as a business manager, be able to 'speak' that language by keeping double entry records.

The following section introduces the concept of double entry accounting.

The basis of any accounting system is the accounting equation.

ASSETS = LIABILITIES + OWNER'S EQUITY

1) ASSETS: Things of value owned by the business i.e. land, buildings, machinery, crop and livestock inventories.

2) LIABILITIES: Debts owed by the business - i.e. accounts payable, mortgages, operating loan.

3) OWNER'S EQUITY: Portion of the business which belongs to the owners.

This accounting equation can be used to describe any type of business whether a lemonade stand or a multinational firm, or of course your farming business.

The equation must always be in balance because the value of the interests in the assets (Liabilities and Owner's Equity) must always be equal to the value of the assets themselves.

Shown graphically, the accounting equation can be shown as the following:

LEFT HAND SIDE	RIGHT HAND SIDE
ASSETS	LIABILITIES
- cattle - land - cash	- operating loan mortgage
	OWNER'S EQUITY
	- capital investment - retained earnings

If you are familiar with a balance sheet (statement of financial position) you may recognize the above format.

The financial structure of a business is constantly changing due to increases and decreases in assets, liabilities and owner's equity. Although the details and dollar amounts of assets, liabilities and owner's equity may change, the form of a business never changes; it will always be:

ASSETS = LIABILITIES + OWNER'S EQUITY

EXAMPLE

In the first year of operation, the financial structure of a business may be shown as the following:

A	=	L	+	OE
$10,000		$2,000		$8,000

After several years of operation the financial structure of the business may have changed to the following:

A	=	L	+	OE
$35,000		$15,000		$20,000

On the following pages, we'll look at how the financial transactions of an individual, "Southern Farmer", effect the accounting equation, A=L+OE, and how this equation always remains in balance.

A) Suppose "Southern Individual" decides to organize and start a farming business by contributing $50,000 cash to the new farming operation. The financial condition of the operation can be expressed by which of the following equations?

1) ASSETS = LIABILITIES + OWNER'S EQUITY
(Cash $50,000) (Capital investment $50,000) ($0)

2) ASSETS = LIABILITIES + OWNER'S EQUITY
(Cash $50,000) ($0) (Capital investment $50,000)

3) ASSETS = LIABILITIES + OWNER'S EQUITY
(Cash $0) ($50,000) (Capital investment $50,000)

(answer to previous question is (2))

B) Now suppose Southern Farmer borrows $6,000 from the bank. Which of the following changes would take place in the amounts shown by the accounting equation?

1) Assets would decrease by $6,000 and owner's equity would increase by $6,000.

2) Liabilities would increase by $6,000 and assets would decrease by $6,000.

3) Both assets and liabilities would increase by $6,000.

4) Assets would increase by $6,000 and liabilities would decrease by $6,000.

5) Both assets and owner's equity would increase by $6,000.

(answer to previous question is (3))

C) Southern Farmer next spends cash for the following items:

Farm Trucks	$20,000
Office Equipment	1,500
	$21,500

THE ACCOUNTING EQUATION:

1) Would not change.

2) Would change by showing an increase in assets of $21,500 and a decrease in owner's equity of $21,500.

3) Would change by showing an increase in assets of $21,500 and an increase in liabilities of the same amount.

4) Would change by showing an increase in assets of $21,500 and an increase in owner's equity of the same amount.

All that really happened in the aforementioned situation was that 'Southern Farmer' traded one form of asset (cash) for other forms of assets (farm trucks and office equipment).

The items making up the total in the account equation at this point are as follows:

ASSETS		=	LIABILITIES		+	OWNER'S EQUITY	
Cash	$34,500		Notes Payable	$6,000		Capital Investment	$50,000
Farm Trucks	20,000						
Office Equip.	1,500						
	$56,000	=		$6,000	+		$50,000

D) 'Southern Farmer' next purchases $1,000 worth of machinery for which he agrees to pay in 30 days. Which of the following changes would take place in the Accounting Equation?

1) There would be no change in totals.

2) Assets would increase and liabilities would decrease.

3) Both assets and liabilities would increase.

4) Liabilities would increase and assets would decrease.

Assets in the form of machinery would increase. Liabilities in the form of accounts payable (which are amounts owed to creditors for items purchased from them) would also increase. The items making up the totals in the accounting equations would now appear as follows:

ASSETS		=	LIABILITIES		+	OWNER'S EQUITY	
Cash	$34,500		Notes	$6,000		Capital Investment	$50,000
Farm Trucks	20,000		Accounts Payable	1,000			
Office Equip.	1,500						
Machinery	1,000						
	$57,000	=		$7,000	+		$50,000

INCOME AND EXPENSE TRANSACTIONS

A farming business is not formed merely to acquire assets through incurring debt or by increasing capital investments. Rather, it intends to use the assets as a means of securing yet a greater amount of assets.

This is accomplished by rendering services (custom work) or selling certain types of assets (inventory, grains, livestock). This is done with the expectation that the assets received in return (usually in the form of cash) will have a greater value than the cost to produce the assets surrendered.

The total flow of services rendered or goods delivered to customers is called Gross Income. Expense is measured in terms of the cost of the assets purchased. The difference between gross income and expenses is Net Income (or Loss). Net income belongs to the owners of the business. Thus, gross income provides a source of assets and as well increases owner's equity.

E) Assume that 'Southern Farm' does custom work for a neighbor and in return receives $2,000 in cash. It is evident that cash increases by $2,000, but what other change would you think is necessary to keep the accounting equation in balance?

1) Liabilities increase by $2,000.

2) Owner's equity increases by $2,000.

3) Other assets decrease so there is no change in total assets.

Customers have given assets to the business in exchange for the services rendered. The growth in assets does not belong to a creditor (outside equity) but serves to increase the owner's equity. This is basically the purpose of every business.

The change would appear as follows:

ASSETS		=	LIABILITIES		+	OWNER'S EQUITY	
Cash	$36,500		Notes payable	$6,000		Capital Farm Investment	$50,000
Trucks	20,000		Accounts payable	1,000		Retained earnings	2,000
Office Equip.	1,500						
Machinery	1,000						
	$59,000	=		$7,000	+		$52,000

The increase in owner's equity is shown as a separate item, "Retained Earnings", and not as a part of capital investment. Retained earnings represent the growth in owners equity due to net income being reinvested in the business.

F) 'Southern Farmer' now sells grain for $900., but does not receive the money immediately. What changes would take place?

1) There would be no change in the totals.

2) Both assets and owner's equity would increase.

3) Both assets and liabilities would increase.

4) Both liabilities and owner's equity would increase.

The correct response should have indicated that assets would increase and owner's equity would increase in the form of retained earnings by $900.

Cash could not be increased as no cash has as yet been received for the grain. However, something of value has been received. This is the claim upon the purchaser of the wheat; the right to collect from him at a later date.

The exact title you employ is not improtant (in accounting terminology, it is called an account receivable). It is important that you recognize the existence of an account receivable as an asset. (The opposite of this is your promise to pay someone at a later date; this would be a liability.)

The accounting equation would appear as follows:

ASSETS		=	LIABILITIES		+	OWNER'S EQUITY	
Cash	$36,000		Notes Payable	$6,000		Capital Accounts	
Accounts			Accounts			Investment	$50,000
Receivable	900		Payable	1,000		Retained	
Farm Trucks	20,000					Earnings	2,900
Office Equip	1,500						
Machinery	1,000						
	$59,900	=		$7,000	+		$52,900

G) Expenses may be looked upon as factors which tend to reduce owner's equity, or more simply, as the costs of doing business. An example of this would be a payment for land rental for the amount of $150. How would the amount in the accounting equation change?

1) Assets would decrease and liabilities would decrease.

2) Assets would decrease and owner's equity would increase.

3) Assets would decrease and owner's equity would decrease.

Incurring expenses tends to off-set the increase in owner's equity caused by the receipt of revenue and reduce assets usually cash by the amount of the payment. What we see now is that the gross revenue of $2,900 has been reduced by $150 of expenses resulting in $2,750 of retained earnings. The accounting equation will now appear as follows:

ASSETS		=	LIABILITIES		+	OWNERS EQUITY	
Cash	$36,350		Notes Payable	$6,000		Capital Investment	$50,000
Receivable	900		Accounts Payable	1,000		Retained Earnings	2,750
Farm Trucks	20,000						
Office Equip.	1,500						
Machinery	1,000						
	$59,750	=		$7,000	+		$52,750

Custom Work	$ 2,000
Grain	900
	$ 2,900
Less Rent	$ 150
	$ 2,750

H) 'Southern Farmer' next pays $3,000 of his $6,000 notes payable. The effect on the accounting equation would be:

1) A decrease in both assets and owner's equity.

2) A decrease in both assets and liabilities.

3) An increase in owner's equity and a decrease in assets.

4) An increase in owner's equity and a decrease in liabilities.

Assets in the form of cash would be decreased and liabilities in the form of notes payable would also be decreased. The transaction did not involve a recognition of revenues or expenses and therefore would not affect owner's equity. The amount in the accounting equation would appear as follows:

ASSETS		=	LIABILITIES		+	OWNER'S EQUITY	
Cash	$33,350		Notes Payable	$3,000		Capital Investment	$50,000
Accounts Receivable	900		Accounts Payable	1,000		Retained Earnings	2,750
Farm Trucks	20,000						
Office Equipment	1,500						
Machinery	1,000						
	$56,750	=		$4,000			$52,750

Custom Work		$ 2,000
Grain		900
Less:	Land Rental	150
		$2,750

1) 'Southern Farmer' collects $900 of the accounts receivalbe which are outstanding for the grain he sold. The changes in the accounting equation would be:

1) The asset, cash, increases and the asset, accounts receivable decreases.

2) The asset, cash, increases and the liability, accounts payable decreases.

3) The asset, cash decreases and the asset, accounts receivable, increases.

This transaction only affects items within the asset catagory. The customer paid cash for the amount he owed. Therefore, cash increases and accounts receivable (amounts customers owe) decreases. There is no change in the total of the assets, the liabilities, or owner's equity.

The amounts in the accounting equation would appear as follows:

ASSETS		=	LIABILITIES		+	OWNER'S EQUITY	
Cash	$34,250		Notes Payable	$3,000		Capital Investment	$50,000
			Accounts Payable	1,000		Retained Earnings	2,750
Farm Trucks	20,000						
Office Equipment	1,500						
Machinery	1,000						
	$56,750	=		$4,000			$52,750

Custom Work		$ 2,000
Grain		900
Less:	Land Rental	150
		$2,750

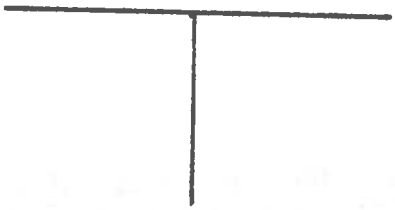
ACCOUNT

When you begin to record financial transactions you will want to group and summarize similiar transactions together. For example, you will want to know the total of all fuel purchases.

Similiar transactions can be grouped together in an account. In your own records you will have many different types of accounts.
i.e. Expense Accounts - Feed, Interest Charges, Fertilizer.
Income Accounts - Cattle, Grain.

The way an account functions can be illustrated through the use of a T Account.

A SIMPLE T ACCOUNT



To determine the net amount of an account, all increases must be entered on one side and all decreases on the opposite side.

A good example of this is your bank account. When you receive your bank statement it may look like the following:

BANK		OPENING BALANCE
Deposit	$1,000	$1,080
Cheque	$100	980
Cheque	$500	480
Cheque	$ 50	430
Deposit	$ 20	450
		Ending balance $450.00

All increases, or deposits are entered on one side and all decreases from your account or cheques are listed on the other side. This allows you to determine the net balance of the account.

The point of keeping double entry books is that it reduces your chance of making an error in arithmetic to nearly zero by enabling you to balance your books. To be able to balance or check your books arithmetically, accounts are divided into two groups in such a way that the total of the balances in one group are equal to that of the other group. You should already be familiar with these two groups of accounts because they are:

ASSETS = LIABILITIES + OWNER'S EQUITY:

With Assets being one group of accounts and the Liabilities and Owner's Equity being the second.

The accounting equation provides two groups of accounts with equal totals. If the transactions have been recorded properly, the total of all asset accounts must equal the total of all liability and owner's equity account.

DOUBLE ENTRY ACCOUNTING

As was just mentioned, accounts are divided into two groups in such a way that the total of the balances in one group is always equal to the total of the balances in the other group.

In one of these groups of accounts, increases are entered on the left side of each account involved and decreased on the right side.

i.e.

ACCOUNT	
1. (increase) $500.00	(decrease) $200.00
	Balance $300.00

In the other group of accounts, increases are entered on the right side of each account and decreases on the left.

ACCOUNT	
2. (decrease) $200.00	(increase) $700.00
	Balance $500.00

The double entry system has an automatic arithmetic check. Every time a transaction is recorded, the left side of one account is affected and the right side of another account is affected.

ACCOUNT 1	
$200.00	

ACCOUNT 2	
	$200.00

As a result, the totals shown for left balance accounts must always equal the total shown for the right balance accounts.

In recording financial transactions in accounts, it's necessary to decide which side of the account shall be used for increases and which side for decreases. The decision is based upon the traditional form of the Balance Sheet (statement of financial position).

And the accounting equation:

ASSETS = LIABILITIES + OWNERS'S EQUITY

BALANCE SHEET

ASSETS	LIABILITIES
	OWNER'S EQUITY

Transactions should be recorded in such a manner that the accounts representing items that commonly appear on the left side of the balance sheet (assets) will have left side balances.

CASH ACCOUNT	
$200.00	

Accounts representing items that appear on the right side of the balance sheet (liabilities and owner's equity) will have right side balances.

BANK LOAN	
	$10,000

OWNER'S EQUITY	
	$30,000

Therefore assets are increased on the left side of the account and decreased on the right side.

CASH ACCOUNT	
(increase) $500.00	$300.00 (decrease)
(balance) $200.00	

Liabilities and owner's equity items will be increased on the right side of the account and decreased on the left side.

BANK LOAN	
(decrease) $5,000	$15,000 (increase)
	$10,000 (balance)

OWNER'S EQUITY	
(decrease) $20,000	$50,000 (increase)
	$30,000 (balance)

Shown below are the entries from the previous examples for 'Southern Farmer', recorded using the double entry method:

ASSETS = LIABILITIES + OWNER'S EQUITY

CASH

(A) 50,000	(C) 21,500
(B) 6,000	(G) 150
(E) 2,000	(H) 3,000
(I) 900	

ACCOUNTS PAYABLE

	(D) 1,000

CAPITAL INVESTMENT

	(A) 50,000

ACCOUNTS RECEIVABLE

(F) 900	(I) 900

NOTES PAYABLE

(H) 3,000	(B) 6,000

RETAINED EARNINGS

(G) 150	(E) 2,000
	(F) 900

FIXED ASSETS

(C) 20,000	
(C) 1,500	
(D) 1,000	

If this procedure is followed for each transaction, the left side entry (or entries) will be equal to the right side entry (entries).

This set of books can now be balanced or checked, to make sure that all transactions have been entered correctly.

1) Total all the columns.

2) Add all left hand column totals together.

3) Add all right hand column totals together.

If the transactions have been recorded properly, left hand totals will equal the right hand columns.

ASSETS = LIABILITIES + OWNER'S EQUITY

CASH

(A) 50,000	(C) 21,500
(B) 6,000	(G) 150
(E) 2,000	(H) 3,000
(I) 900	

ACCOUNTS PAYABLE

	(D) 1,000

CAPITAL INVESTMENT

	(A) 50,000

ACCOUNTS RECEIVABLE

(F) 900	(I) 900

NOTES PAYABLE

(H) 3,000	(B) 6,000

RETAINED EARNINGS

(G) 150	(E) 2,000
	(F) 900

FIXED ASSETS

(C) 20,000	
(C) 1,500	
(D) 1,000	

$82,300	$25,550	$ 3,000	$ 7,000	$ 150	$52,900

Left hand side

$82,300
3,000
150
$85,450

=

Right hand side

$25,550
7,000
52,900
$85,450

This is the fundamental basis of double-entry accounting and results from the basic accounting equation A=L+OE. The use of the two sides of the various kinds of accounts may be stated graphically as follows:

A		=	L		+	OE	
INCREASE	DECREASE		DECREASE	INCREASE		DECREASE	INCREASE
+	-		-	+		-	+

Assets normally have balances on the:

1) Left side of the "T Account".

2) Right side of the "T Account".

Liabilities and owner's equity accounts normally have balances on the:

1) Left side of the "T Account".

2) Right side of the "T Account".

Entering an amount on the left side of an account does which of the following?

1) Increase an owner's equity account.

2) Decreases an asset account.

3) Decreases a liability account.

The complete analysis of transaction in terms of their effect on different kinds of accounts may be summerized in the equation presented below:

ASSETS		=	LIABILITIES		+	OWNER'S EQUITY	
INCREASE +	DECREASE -		DECREASE -	INCREASE +		DECREASE -	INCREASE +

EXPENSES		REVENUE	
Inc.	Dec.	Dec.	Inc.
+	-	-	+

DEBIT AND CREDIT DEFINED

In accounting language, debit only refers to the left side of any account.

The word credit only refers to the right side of any account. These words don't have any other type of meaning. The illustrations below show each type of account with respect to the rules of debit and credit.

ASSETS = LIABILITIES + OWNER'S EQUITY

AN ASSET ACCOUNT

Debit	Credit
+	-
Inc.	Dec.

A LIABILITY ACCOUNT

Debit	Credit
+	-
Dec.	Inc.

CAPITAL INVESTMENT ACCOUNT

Debit	Credit
+	-
Dec.	Inc.

EXPENSE ACCOUNT

Debit	Credit
+	-
Inc.	Dec.

REVENUE ACCOUNT

Debit	Credit
-	+
Dec.	Inc.

The above graphic illustrations is sometimes called the Rule of Double Entry.

WHY THE BANK IS BACKWARDS

Throughout the previous section, you were told that your bank account was one of your assets, and because of that, all the increases to that account were entered on the left (Debits) and all the decreases were on the right (Credits).

This explanation satisfies most people until they look at their bank statement. On the statement, the above rule seems to be reversed, as the example below show. Why is this?

BANK STATEMENT

DESCRIPTION	DEBITS	CREDITS	DATE DAY	DATE MO	250.00 BALANCE
CHEQUE 100	12.00				238.00
CHEQUE 101	100.00				138.00
CHEQUE 102	50.00				88.00
DEPOSIT		200.00			288.00
CHEQUE 103	10.00				278.00
SERVICE CHARGE	5.00				273.00

The reason for this is that the statement you receive from the bank is a statement of their account with you, and when you deposit money with the bank, they owe you that money; Of course everyone knows by now that in a liability account, increases are shown on the right (Credits) and decreases are shown on the left (Debits) - just the way it appears on your bank statements.

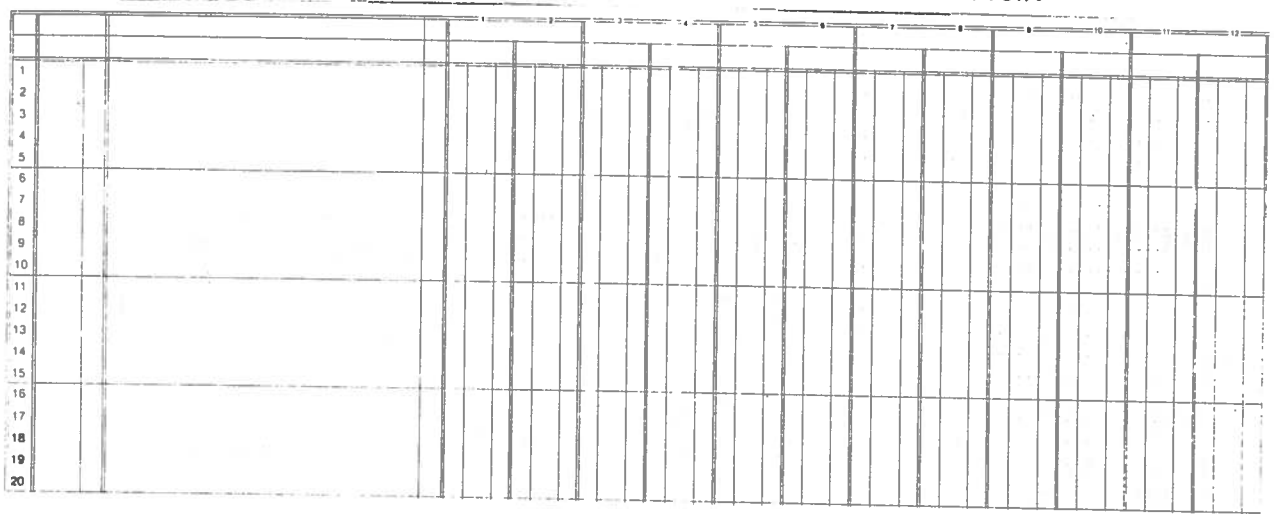
In your own records, you will want to show your bank account as an asset. You will record increases to your bank as debits, and decreases as credits.

SETTING UP A RECORD BOOK

Synoptic Journal

For keeping double entry farm records a blank accounting book called a synoptic journal can be used. Synoptic means 'all encompassing' so a synoptic journal is one where all your accounts are recorded. These journals are available in varying sizes up to 36 columns wide.

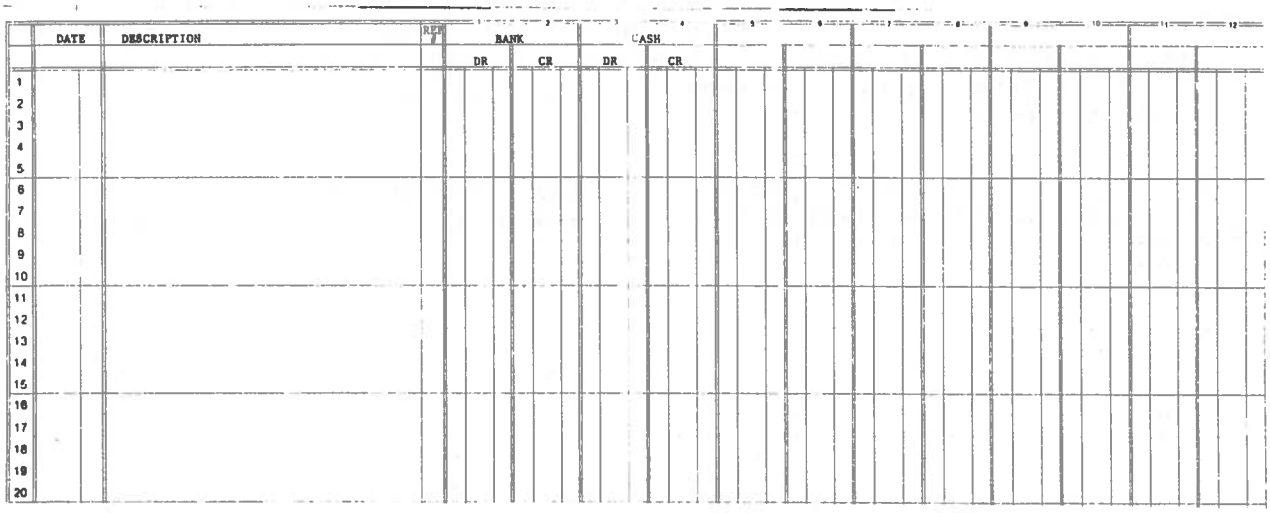
The first page of a blank 30 column journal is shown below:



The first columns to be labelled are the ones for Date, Description, and Reference Number (abbreviated Ref#). Ref # refers to the cheque or deposit number of each transaction.

The previous section on double entry accounting showed that every business has Asset, Liability and Owners Equity accounts. These accounts are set up in this same order across the page on your synoptic journal. Assets accounts are listed first.

The Asset accounts that you will record changes in most frequently are your Bank Account and a Cash Account (if you have cash transactions). It's necessary to record increases and decreases in each of these accounts, so both must have a Debit and Credit side. The abbreviations for Debit and Credit are DR and CR.



You will then want to have two columns labelled for Loans, this will enable you to record all increases or decreases in your loan accounts. Although you may have more than one loan, for the sake of saving space, all loan transactions can be grouped for now under one account.

	DATE	DESCRIPTION	REF	BANK		CASH		LOANS											
				DR	CR	DR	CR	DR	CR										
1																			
2																			
3																			
4																			
5																			
6																			
7																			
8																			
9																			
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15																			
16																			
17																			
18																			
19																			
20																			

The majority of the accounts you need will be Owner Equity accounts. These include all your Revenue and Expense accounts.

Until now accounts have always been shown as T accounts; that is an account with two sides so that decreases and increases to an account can be recorded. However for many accounts it is only necessary to use one side of a T account. The reason for this is that you only need to be recording increases to these accounts throughout the year. For instance you will always be buying more fuel or selling more cattle, not returning fuel or accepting back cattle. For expenses you need only a Debit(DR) column and for revenue you will need a Credit (CR) column

The following example shows expense accounts for fertilizer, fuel, repairs, and revenue accounts for cattle and grain.

	DATE	DESCRIPTION	REF	BANK		CASH		LOANS		FERT.	FUEL	MACHINERY REPAIRS	CATTLE SALES	[illegible]
				DR	CR	DR	CR	DR	CR	DR	DR	DR	CR	CR
1														
2														
3														
4														
5														
6														
7														
8														
9														
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11														
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17														
18														
19														
20														

Another necessary Owner Equity account is a personal account to keep track of any owners contributions or withdrawals to the business.

			BANK		CASH		LOANS		FERT.	FUEL	MACHINERY REPAIRS		CATTLE SALES	GRAIN SALES	PERSONAL			
			DR	CR	DR	CR	DR	CR	DR	DR	DR		CR	CR	DR	CR		
1																		
2																		
3																		
4																		
5																		
6																		
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19																		
20																		

The final account to enter is called the General Ledger account. This is a 'catch-all' type of account where any miscellaneous transactions can be recorded. Capital Asset purchases and disposals can also be recorded in this account since these transactions usually do not occur often enough to warrant a separate account.

			BANK		CASH		LOANS		FERT.	FUEL	MACHINERY REPAIRS		CATTLE SALES	GRAIN SALES	PERSONAL		GENERAL LEDGER	
			DR	CR	DR	CR	DR	CR	DR	DR	DR		CR	CR	DR	CR	DR	CR
1																		
2																		
3																		
4																		
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19																		
20																		

Note that the arrangement of these accounts in your journal follows the pattern of the accounting equation of:

ASSETS	=	LIABILITIES	+	OWNERS EQUITY

Bank		=	Loans		+	Fert.	Cattle	Personal	
DR	CR		DR	CR		DR	CR	DR	CR
Cash		=			+	Fuel	Grain	Gen.Led.	
DR	CR					DR	CR	DR	CR
						Repairs			
						DR			

The only difference is that in the accounting book the accounts are arranged horizontally.

Accounts For Your Own Records

To determine the accounts you would need for your own records, look at your present accounting book or check your latest income tax return which will have your income and expense headings. The Farmers and Fishermans Tax Guide indicates headings you can use or you can check with your accountant.

Consider your own situation carefully, you may want to keep track of special types of accounts for your own purposes. For example, you may want to have accounts for repairs on individual pieces of equipment, or you may want to break down expenses between different enterprises.

Exercise I

In the following example, the accounts to be kept are:

Assets:	Bank Cash	
Liabilities:	Loans	
Owners Equity:	Expenses	Income
	Machinery Repair Truck Repair Gas & Oil Car Expenses Hardware & Tools Interest & Service Charges Feed Freight & Trucking Fertilizer Cattle Purchases Utilities Insurance & Licenses Sprays & Chemicals Salaries Crop Supplies Building Repair	Cattle Sales Wheat CWB Payment Customs Work
	Others	
	Personal General Ledger	

Arranged on a 30 column journal page, these accounts would look like the following:

	DATE	DESCRIPTION	REF #	BANK DR	BANK CR	CASH DR	CASH CR	LOANS DR	LOANS CR	MACHINERY R&M DR	TRUCK R&M DR	GAS & OIL DR	CAR EXPENSE DR	HARDWARE & TOOLS DR	Fed & S.C. CR
1															
2															
3															
4															
5															
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7															
8															
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22															
23															
24															
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26															
27															
28															
29															
30															

	Feed DR	TRUCKING DR	FERT. DR	CATTLE PURCHASES DR	UTILITIES DR	LICENSE INSURANCE DR	SPRAYS CHEMICALS DR	SALARY DR	CROP SUPPLIES DR	BUILDING R & M DR	CUSTOM WORK CR	CATTLE SALES CR	WHEAT CR	C.W.B. PAYMENT CR	PERSONAL DR	PERSONAL CR	GENERAL LEDGER DR	GENERAL LEDGER CR
1																		
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RECORDING FINANCIAL TRANSACTIONS

With all the preliminaries covered you are almost ready to begin recording financial transactions.

When you sit down to do your books make sure you are comfortable - have enough space to accommodate all your papers.

You'll need: journal
bank statement & cancelled cheques
invoices

Also: calculator
ruler
highlighter pen (useful, but not necessary)

The procedure to follow for recording is outlined below; the actual method for entering a specific transaction will be discussed later.

1) Record all cheques first.
- do in numerical order with the information from your cheque stubs.
- record every cheque that you wrote regardless of whether it has been cashed yet.
- look at each invoice as you record
- this is a good time to make sure that you haven't overpaid a bill.
- after each transaction check off the corresponding entry on the bank statement.
- keep track of the cheques which you have recorded but are outstanding (the purpose of checking everything off on the bank statement is so that you can make sure eventually that everything that passes through the bank is recorded).

2) Deposits:
- record in order from the deposit book.
- match to receipt
- you want to make sure you received the right amount of income.
- check off on your bank statement.

3) Debit Memos:
-these are:
  - loan payments
  - transfers to another account
  - service charges
  - interest charges
- record from the bank statement
- check them off on the bank statement as you record them.

4) Credit Memos:
- these are:
  - loan advances
  - transfers from another account
- record from the bank statement
- check them off on the bank statement as you record them.

5) Cash Transactions.

6) Reconcile your books to your bank account
- this is the final check; it can be done on a separate sheet of paper and attached to your journal page.

7) Balance your Journal
- to balance:
  a) total every column
- write the total at the bottom
  b) add the total of each Debit column
  c) add the total of each Credit column
  d) the total of all the Debit columns must equal the total of all the Credit columns.
- if your books don't balance; you must locate the error.
- find the amount of the difference between your Debit and Credit columns
- this will help you discover where your error is.

When you begin to record next month, your first step will be to check off on that month's bank statement any cheques that were recorded previously but returned with the current bank statement.

ENTERING TRANSACTIONS

When done properly, your books will give you an exact summary of where your money has come from and where it has gone.

There are two sides to every financial transaction; the money has originated from somewhere and been used somewhere else. Remember this when you record transactions.

Recording Cash Outflow

There are four major kinds of cash outflow that you will record:

1) Farm operating expenses. These are items purchased for the business of farming and usually used within one year. i.e. fuel, fertilizer.
2) Capital expenses. These are purchases of fixed assets. i.e. machinery, buildings.
3) Debt payments. These are loan repayments. The principal portion is the debt payment, the interest on the loan is an operating expense.
4) Personal withdrawals. These are items for personal consumption.

Example
You wrote a cheque for $45.00 for equipment parts. What has happened?

You have decreased your bank account by $45.00 and increased your equipment expenses by the same amount.

How is that recorded?

Your bank account is an asset (remember, assets are on the left side of the balance sheet so they are increased on the left and decreased on the right) so you make a $45.00 entry under the Bank CR. column.

An expense account is an owner equity account (on the right side of the balance sheet, therefore it is increased on the right and decreased on the left) and you have decreased your equity. The entry is made under the DR column under Equipment Repair Expense.

	DATE	DESCRIPTION	REF	BANK DR	BANK CR	CASH DR	CASH CR	EQUIPMENT REPAIR DR
1	JAN 2	A.B.C. SUPPLY LTD.	319		45 00			45 00
2								
3								
4								
5								
6								
7								
8								
9								
10								
11								
12								
13								
14								
15								
16								
17								
18								
19								
20								

Recording Cash Inflow

There are four major kinds of cash inflow that you will record:

1) Farm Income - Income received from the sale of farm products.
2) Capital Sales - Income received from the disposal of fixed assets.
3) Loan Advances - Money deposited into your bank account for an operating or other type of loan advance.
4) Personal Income - Income received from personal sources such as off farm employment.

Example:
If you had to record a deposit for $7,500.00 under cattle sales it would be done the following way.

	DATE	DESCRIPTION	REF	BANK DR	BANK CR	CASH DR	CASH CR	EQUIPMENT REPAIRS DR	CATTLE SALES CR
1	FEB 21	TIGHT FISTED AUCTION MART	DJ	750 0 00					750 0 00
2									
3									
4									
5									
6									
7									
8									
9									
10									
11									
12									
13									
14									
15									
16									
17									
18									
19									
20									

Your DR and CR entries must balance for each transaction.

Other Points

- Fill in the date of each transaction.
- Use the 'Description' column for recording who the cheque was written to, or from whom income was received.
- In the Reference # column, enter the number of the cheque or deposit.
- Miscellaneous items can be entered in the General Ledger columns;
- Capital purchases and sales can also be entered in the General Ledger columns.
- If you feel you need to write down an extra explanation about a transaction do it in your books - this saves you time later.
- If you need more than one page per month, total the columns of the first page, make sure they cross balance, and then carry the column totals to the top of the same column on the next page.
- Similar transactions can be entered in different ways in your books and still be correct. The important thing to remember is to be consistent in the method you choose to enter a transaction. If you do it one way once, keep doing it that way. Also, if you aren't sure how to enter a transaction, you can check with your accountant to see how he would like it to appear in your books.

RECORDING OTHER TRANSACTIONS

You may have to enter some transactions which are different from those covered in the previous exercise.

1) Prepaid Accounts
If you deposit money with a dealer that is used up as you purchase parts or supplies through the year, the entries for your records could be handled in the following way:

example you give the dealer a cheque for $500., and later obtain a total of $450., worth of parts.

	DATE		DESCRIPTION	REF	BANK DR	BANK CR	CASH DR	CASH CR	EQUIPMENT REPAIRS DR	GENERAL LEDGER DR	GENERAL LEDGER CR
1	JAN	5	LOCAL DEALER LTD.	320		500 -				500 -	
2										(to prepaid account)	
3	Jan	29	PARTS FROM LOCAL DEALER						150 -		150 -
4										(from prepaid account)	
5	May	7	PARTS FROM LOCAL DEALER						75 -		75 -
6										(from prepaid account)	
7	Sep	16	PARTS FROM LOCAL DEALER						225 -		225 -
8										(from prepaid account)	
9											
10											
11											
12											
13											
14											
15											
16											
17											
18											
19											
20											

- note: you still have a balance owing to you of $50.00.

2) Returns for Credit.
If you purchase supplies which you later return for credit from the suppliers you would enter it the following way:

a) purchase supplies
b) returned supplies - received 'credit' from supplier
c) purchased more supplies to use up 'credit'

	DATE		DESCRIPTION	REF	BANK DR	BANK CR	CASH DR	CASH CR	FARM SUPPLIES DR	GENERAL LEDGER DR	GENERAL LEDGER CR
1		a)	A.B.C. SUPPLY LTD	321		325			325 -		
2											
3		b)	RETURNED SUPPLIES						(325 -)	325 -	
4										(account with A.B.C. Supply)	
5		c)	PURCHASED SUPPLIES FROM A.B.C.						250 -		250 -
6										(reducing account with A.B.C.	
7											
8											
9											
10											
11											
12											
13											
14											
15											
16											
17											
18											
19											
20											

note: you would still have a balance owing to you of $75.00 at A.B.C. Supply.

3) Capital Purchase with loan and trade in. Often with the purchase of new equipment or machinery, a down payment is made, an older piece of equipment is traded in and a loan is incurred.

In the following example a new tractor worth $65,000 is purchased, an older tractor worth $25,000 is traded in, a down payment of $10,000 is made and the balance owing is held as a loan with the dealer.

	DATE	DESCRIPTION	REF	BANK DR	BANK CR	LOANS DR	LOANS CR	GENERAL LEDGER DR	GENERAL LEDGER CR
1		HONEST ERNIES TRACTORS	322		10000 -		30000	65000 - NEW TRACTOR	25000 - OLD TRACTOR
2									
3									
4									
5									
6									
7									
8									
9									
10									
11									
12									
13									
14									
15									
16									
17									
18									
19									
20									

4) Capital Purchase with no down payment and interest free.

Equipment dealers sometimes will make a special offer to sell equipment with no down payment required and the balance interest free until later.

If you agree to purchase equipment in this way, you will take possession of the item but no financial transaction has been recorded. The transaction should be entered in you books however, or you may miss claiming the Capital Cost Allowance and Investment Tax Credit of the new equipment.

You would show that you purchased a new fixed asset, and that you incurred a loan with the dealer. For a $50,000 tractor, the transaction would be entered the following way:

	DATE	DESCRIPTION	REF	BANK DR	BANK CR	LOANS DR	LOANS CR	GENERAL LEDGER DR	GENERAL LEDGER CR
1	NOV 29	HONEST ERNIES'S TRACTORS	323				50000 -	50000 - (NEW TRACTOR)	
2									
3									
4									
5									
6									
7									
8									
9									
10									
11									
12									
13									
14									
15									

5) Recording Total Income and Marketing Costs.

When you sell cattle and grain, deductions for marketing and other costs are often made from the gross amount of the cheque. You receive the net amount.

To record the net amount of the cheque as your income would not be incorrect. However to get a better idea of your total income you could record the gross amount of the cheque and the corresponding deductions.

for example: you sold cattle for $10,500 and the commission charge of $300.00 was deducted on the cheque.

	DATE		DESCRIPTION	REF #	BANK DR	BANK CR			MARKETING COSTS DR		CATTLE SALES CR	
1	MAR	21	TIGHT FISTED AUCTION MART	D4	10200	-			300	-	10500	-
2												
3												
4												
5												
6												
7												
8												
9												
10												
11												
12												
13												
14												
15												
16												
17												
18												
19												
20												

6) Recording Patronage Payments.

You may receive patronage payments from cooperatives. Usually the payment shows a gross amount of dividend and certain deductions are made from it to leave you with a net amount. Deductions are usually to increase the value of your share in the cooperative and income tax that is withheld.

for example: You received a patronage payment for $50.00. The actual amount of income was $80.00 but $10.00 was used to increase your share and $20.00 was withheld as income tax.

DATE	DESCRIPTION	REF #	BANK DR	BANK CR	DIV. INCOME CR	DIV. INCOME DR	GENERAL LEDGER DR	GENERAL LEDGER CR
NOV 1	Co-op Patronage Payment	D5	50.00		80.00		10.00 (share value) 20.00 (witheld tax)	

The completed journals from the exercises would look like the following.

EXERCISE I

	DATE		DESCRIPTION	REF	BANK DR	BANK CR	CASH DR	CASH CR	LOANS DR	LOANS CR	MACH R&M DR	TRUCK R&M DR	GAS & OIL DR	CAR EXPENSE DR	HARDWARE TOOLS DR	INT & SC DR
1	NOV	1	PROPELLANT FUELS	213		176 8 -							17 68 -			
2	"	1	FIXIT MOTORS	214		69 5 -						6 95 -				
3	"	3	WHATEVER YOUR NEEDS HARDWARE	215		2 4 -									2 4 -	
4	"	5	KEEP YOUR PLANTS HAPPY FERTILIZER	216		1 00 00 -										
5	"	12	EASY MONEY AUCTION MART	217		5 42 58 -										
6	"	13	AGGRAVATING PHONE SERVICE	218		2 6 -										
7	"	18	TRY COLLECT INSURANCE	219		6 36 -										
8	"	19	COOL THREADS MEN'S WEAR	220		3 71 -										
9	"	20	KILL EM DEAD CHEMICALS	221		15 00 -								1 08 -		
10	"	24	HAPPY VALLEY COUNTY	222		14 33 -										
11	"	27	GROW EM QUICK FEED MILLS	223		24 78 -										
12	"	29	CULTIVATE RIGHT FARM SUPPLIES	224		1 00 00 -										
13	"	30	FIXIT MOTORS	225		96 -										
14	"	25	OPERATING LOAN PAYMENT	DM		32 0 00 -								9 6 -		
15	"	25	INTEREST	INT		80 5 56			32 000 -							
16	"	30	SERVICE CHARGE	SC		2 80										80 5 56
17	"	4	STORE YOUR OWN GRAIN - WHEAT	D16	22 0 50 -											2 80
18	"	22	TIGHT FISTED AUCTION	D17	32 8 08 -											
19	"	15	OPERATING LOAN - ADVANCE	LN	50 0 00 -					5 0 000 -						
20	"	29	A.F.D. LOAN - TRACTOR	LN	10 0 00 -					1 0 000 -						
21																
22					114 8 58 -	116 09 3 36			32 000 -	6 0 000 -		69 5 -	17 68 -	2 04 -	24 -	80 8 36

EXERCISE II

	DATE		DESCRIPTION	REF	BANK DR	BANK CR	CASH DR	CASH CR	LOANS DR	LOANS CR	MACH R&M DR	TRUCK R & M DR	GAS & OIL DR	CAR EXPENSE DR	HARDWARE TOOLS DR	INT & SC DR
1	DEC	1	SMOOTH RIDE TIRES	226		56 9 32						569 32				
2	"	3	HONEST ERNIE'S	227		43 5 79										
3	"	4	JIM OVERWORKED	228		2 50 -										
4	"	6	FIT RITE BEARINGS	229		4 5 19					45 19					
5	"	7	FIXIT MOTORS	230		38 3 5 29					38 35 29					
6	"	10	PROPELLANT FUELS	231		1 238 27										
7	"	13	KEEP EM UNDER FINANCED DEV. CORP.	232		190 7 2 69			3 105 49				743 89	4 94 38		
8	"	20	PULL ANYTHING LTD.	233		120 0 0 -										159 67 20
9	"	21	SUCCULENT FOODS	234		28 5 3 31										
10	"	21	CO-OP	235		4 8 472										
11	"	23	ALOOF ACCOUNTING	236		8 0 0 -							5 6 25		125 06	
12	"	28	ALWAYS DELIVER TRUCKING	237		5 1 3 -										
13	"	29	BUILD IT RIGHT LUMBER CO.	238		7 93 67										
14	"	8	OPERATING LOAN PAYMENT	LP		2 00 0 0 -			20 000 -							
15	"	10	F.I.L. TRUCK	LP		54 7 9 63			39 53 -							
16	"	31	OPERATING LOAN PAYMENT	LP		2 80 0 0 -			28 0 0 0 -							152 6 63
17	"	31	TRANSFER TO 130-503	TF		25 00 -										
18	"	31	INTEREST	INT		62 37										
19	"	31	INTEREST	INT		3 38 33										
20	"	31	SERVICE CHARGE	SC		220										62 37
21	"	4	TIGHT FISTED AUCTION MART - Joe Siesta	D18	3 3 19 0 27											338 33
22	"	23	CWB - FAMILY ALLOWANCE-STORE YOUR OWN GRN	D19	3 4 95 9 75											2 20
23	"	31	STORE YOUR OWN GRAIN	D20	2 1 93 1 02											
24	"	14	OPERATING LOAN ADVANCE	LN	2 0 0 0 -					2 0 0 0 0 -						
25	"	20	F.I.L. TRACTOR	LN	1 0 0 0 0 -					1 0 0 0 0 -						
26	"	18	HONEST ERNIES	CASH				8 5 36								
27	"	21	(return)	CASH			2 5 27									
28	"	21	RETURN HARDWARE - CO-OP	CASH			60 09								60 09	
29																
30																
31					120 0 91 04	9 92 73 78	8 5 36	85 36	55 058 49	3 0 000 -	3 880 48	5 69 32	800 14	4 94 38	64 97	178 94 73
32					234 9 19 04	215 367 14	8 5 36	85 36	87 058 49	9 0 000 -	3 880 48	12 64 32	2 568 14	6 98 38	88 97	187 05 09
33																
34																
35																

	13 Feed DR	14 Freight Trucking DR	15 Fert. DR	16 Cattle Purchase DR	17 Utilities DR	18 Insurance License DR	19 Sprays Chemical DR	20 Salaries DR	21 Crop Supplies DR	22 Building R & M DR	23 Custom Work DR	24 Cattle Sales CR	25 Wheat CR	26 C.W.B. Payments CR	27 Personal DR	28 Personal CR	29 General Ledger DR	30 General Ledger CR
1																		
2																		
3																		
4			10000 -															
5				54258 -														
6					26 -													
7						528 -												
8							1500 -											
9															371 -			
10																PROPERTY	TAXES	
11	2478 -																1433 -	
12																		
13																	20000 -	10000 -
14																	new disc	old disc
15																		
16																		
17													22050 -					
18																		
19												32808 -						
20																		
21	2478 -		10000 -	54258 -	26 -	528 -	1500					32808 -	22050 -		371 -		21433 -	10000 -
22																		

	13 Feed DR	14 Trucking DR	15 Fert. DR	16 Cattle Purchase DR	17 Utilities DR	18 Insurance Licenses DR	19 Sprays Chemicals DR	20 Salaries DR	21 Crop Supplies DR	22 Building R.&M. DR	23 Customs Work DR	24 Cattle Sales CR	25 Wheat CR	26 C.W.B. Payments CR	27 Personal DR	28 Personal CR	29 General CR	30 Ledger DR
1																		
2																		
3																	AIR COMPRESSOR	
4								250 -									435 79	
5																		
6																		
7																		
8																		
9																	NEW TRACTOR	USED TRACTOR
10																	540 00 -	420 00 -
11									270 31						2353 31			
12		513 -													33 10		ACCOUNTING	
13																	800 -	
14										793 67								
15																		
16																		
17																		
18																	TRANSFER	
19																	2500 -	
20																		
21																		
22											5500 -	27690 27						
23													30703 43	41973 6				
24																58 96		
25													21931 02					
26																		
27										85 36								
28										(25 27)								
29		513 -																
30	2478 -	513 -	10000 -	54258 -	26 -	528 -	1500 -	250 -	270 31	853 76	5500 -	27690 27	52634 45	41973 6	2886 41	58 96	57735 79	42000 -
31								250 -	270 31	853 7-	5500 -	60498 27	74684 45	41973 6	3257 41	58 96	79168 79	52000 -
32																		
33																		
34																		
35																		

YEAR END PROCEDURES
-WORK SHEET-

The accounting process consists of three major steps. These are:

1) Recording transactions during the fiscal period and making sure these records are balanced and reconciled.
2) Summarizing all the information at the end of the fiscal period.
3) Reporting and interperting the summarized information in financial statements, (balance sheet and income statement).

You have completed the first step of the accounting process. This information can now be summarized and finalized for the year. This is done by using a work sheet.

A work sheet is an accountant's tool and involves completing several intermediary steps between the journal records and the preparation of formal financial statements. Most people do not do this step on their own but it is a useful exercise to work through now to see how financial statements are prepared.

The 10 columns of a work sheet are labelled in the following way:

SOUTH FARMS
WORK SHEET

TRIAL BALANCE		POSTINGS		ADJUSTING ENTRIES		INCOME STATEMENT		BALANCE SHEET	
DR	CR	DR	CR	DR	CR	DR	CR	DR	CR

A completed work sheet shows:
- the beginning of the year financial status of the business in the Trial Balance columns.
- the financial transactions that occurred during the year in the 'Posting' and 'Adjusting Entries' columns.
- the income and expenses and net income or loss for the year in the 'Income Statement' columns.
- the end of the year financial status of the business in the 'Balance Sheet' columns.

The following exercise works through the steps of a work sheet for South Farms.

1) Total the monthly account column totals on the journal sheets to arrive at a yearly total.

2) Enter the following account names on the left hand side of the work sheet.

Cash
Bank
Savings
Grain
Feed
Cattle
Land
Buildings (Class 6)
Machinery (Class 8)
Power Equipment (Class 10)
Accumalated Capital Cost Allowance
Investment Tax Credit

Operating Loan
F.I. Loan - Truck
F.I. Loan - Tractor
A.F.D. Loan - Disc
Land Loan

Owner's Equity
Owner's Contribution
Owner's Withdrawls
Machinery R & M
Truck R & M
Gas, Oil, etc
Car Expenses
Hardware & small tools
Interest, S/C etc
Feed & straw
Freight & trucking
Fertilizer
Cattle purchases
Utilities
Insurance, Licenses, etc
Sprays & Chemicals
Salaries & Wages
Crop Supplies
Building R & M
Accounting & Legal fees
Custom Work
Cattle Sales
Wheat Sales
C.W.B. payments
Property taxes
Capital Cost claimed.

3) Trial Balance

These figures are the beginning of the year balance sheet account (assets, liabilities and owner's equity) for the business.

	TRIAL BALANCE	
	DR	CR
Cash	0.00	
Bank	2,467.39	
Savings	10,400.00	
Grain	60,000.00	
Feed	10,000.00	
Cattle	59,577.00	
Land	180,000.00	
Buildings	85,528.75	
Machinery	58,255.31	
Power Equipment	106,321.18	
Accumulated Capital Cost Allowance		73,849.59
Investment Tax Credit	4,321.25	
Operating Loan		80,000.00
FIL - Truck		13,275.08
FIL - Tractor		
AFDL - Disc		
KEUDF - Loan		168,075.84
Owner's Equity		241,670.37
Owner's Contributions		
Owner's Withdrawals		
Machinery Repairs & Maintenance		
Truck Repairs & Maintenance		
Gas, Oil, etc.		
Auto Expenses		
Hardware & Small Tools		
Interest, S/C, etc.		
Feed & Straw		
Freight & Trucking		
Fertilizer		
Cattle Purchases		
Utilities		
Insurance, Licenses, etc.		
Sprays & Other Chemicals		
Salaries & Wages		
Crop Supplies		
Building Rep. & Maint.		
Custom Work		
Cattle Sales		
Wheat Sales		
C.W.B. Payments		
Property Taxes		
Accounting & Legal Fees		
Capital Cost Claimed		
TOTALS	576,870.88	576,870.88

4) Posting

This involves taking the yearly totals of each account from the synoptic journal and transferring them to the work sheet.

If an account has a Debit total in the journal, that amount transfers to the Debit column on the work shee .

example

	DATE		DESCRIPTION	REF	BANK DR	BANK CR	CASH DR	CASH CR	LOANS DR	LOANS CR	MACH R&M DR	TRUCK R & M DR	GAS & OIL DR	CAR EXPENSE DR	HARDWARE TOOLS DR	FOR S.C. DR
1	DEC	1	SMOOTH RIDE TIRES	226		569 32						569 32				
2	"	3	HONEST ERNIE'S	227		435 79										
3	"	4	JIM OVERWORKED	228		250 -										
4	"	6	FIT RITE BEARINGS	229		45 19										
5	"	7	FIXIT MOTORS	230		38 35 29					45 19					
6	"	10	PROPELLANT FUELS	231		1 238 27					3 835 29					
7	"	13	KEEP EM UNDER FINANCED DEV. CORP.	232		190 7 69							743 89	4 94 38		
21	"	4	TIGHT FISTED AUCTION MART - Joe Siesta	D18	3 319 027				3 105 49							159 67 80
22	"	23	CWB - FAMILY ALLOWANCE-STORE YOUR OWN GRN	D19	3 495 975											
23	"	31	STORE YOUR OWN GRAIN	D20	2 193 102											
24	"	14	OPERATING LOAN ADVANCE	LN	2 000 -					2 000 00 -						
25	"	20	F.I.L. TRACTOR	LN	1 000 -					1 000 00 -						
26	"	18	HONEST ERNIES	CASH				85 36								
27	"	21	(return)	CASH			25 27									
28	"	21	RETURN HARDWARE - CO-OP	CASH			60 09								60 09	
29																
30					120 081 04	92 73 78	85 36	85 36	55 058 49	0 000 -	3 880 48	569 32	800 14	4 94 38	64 97	178 96 73
31					234 939 04	215 367 14	85 36	85 36	87 058 49	0 000 -	3 880 48	2 64 32	2 568 14	6 98 38	88 97	187 05 09

	TRIAL BALANCE DR	TRIAL BALANCE CR	POSTING DR	POSTING CR	ADJUSTING ENTRIES DR	ADJUSTING ENTRIES CR	INCOME STATEMENT DR	INCOME STATEMENT CR	BALANCE SHEET DR	BALANCE SHEET CR
Cash	0.00									
Bank	2,467.39		234,939.04	215,367.14						
Savings	10,400.00									
Grain	60,000.00									
Feed	10,000.00									
Cattle	59,577.00									
Land	180,000.00									
Buildings	85,528.75									
Machinery	58,255.31									
Power Equipment	106,321.18									
Accumulated Capital Cost Allowance		73,849.59								
Investment Tax Credit	4,321.25									
Operating Loan		80,000.00								
FIL - Truck		13,275.08								
FIL - Tractor										
AFDL - Disc										
KEUDF - Loan		168,075.84								
Owner's Equity		241,670.37								
Owner's Contributions										
Owner's Withdrawals										
Machinery Repairs & Maintenance										
Truck Repairs & Maintenance										
Gas, Oil, etc.										
Auto Expenses										
Hardware & Small Tools										
Interest, S/C, etc.										
Feed & Straw										
Freight & Trucking										

After you have transferred an iten from the journal, put a (x) mark below it.

Loan and general ledger transactions in the journal are analyzed and posted individually. Recall that several loan accounts were grouped in the two loan columns and that the general ledger columns were used for various types of accounts.

example

	DATE		DESCRIPTION	REF #	BANK DR	BANK CR	CASH DR	CASH CR	LOANS DR	LOANS CR	TRACTOR R&M DR	TRUCK R & M DR	GAS & OIL DR	CAR EXPENSE DR	HARDWARE TOOLS DR	FEES + S C DR
1	DEC	1	SMOOTH RIDE TIRES	226		569 32										
2	"	3	HONEST ERNIE'S	227		435 79						569 32				
3	"	4	JIM OVERWORKED	228		250 –										
4	"	6	FIT RITE BEARINGS	229		45 19					45 19					
5	"	7	FIXIT MOTORS	230		3835 29					3835 29					
6	"	10	PROPELLANT FUELS	231		1238 27										
7	"	13	KEEP EM UNDER FINANCED DEV. CORP.	232		1907 269			3105 49				743 89	4 94 08		
8	"	20	PULL ANYTHING LTD.	233		1200 0 –										159 67 20
9	"	21	SUCCULENT FOODS	234		28 53 31										
10	"	21	CO-OP	235		48 472										
11	"	23	ALOOF ACCOUNTING	236		800 –							5 6 25		125 06	
12	"	28	ALWAYS DELIVER TRUCKING	237		511 –										
13	"	29	BUILD IT RIGHT LUMBER CO.	238		793 67										
14	"	8	OPERATING LOAN PAYMENT	LP		2000 0 –			20000 –							
15	"	10	F.I.L. TRUCK	LP		54 79 63			39 53 –							
16	"	31	OPERATING LOAN PAYMENT	LP		2800 0 –			28000 –							1526 63
17	"	31	TRANSFER TO 130-503	TF		25 00 –										
18	"	31	INTEREST	INT		62 37										62 37
19	"	31	INTEREST	INT		338 33										338 33
20	"	31	SERVICE CHARGE	SC		220										2 20
21	"	4	TIGHT FISTED AUCTION MART - Joe Siesta	D18	3 19 0 27											
22	"	23	CWB - FAMILY ALLOWANCE-STORE YOUR OWN GRN	D19	3 495 975											
23	"	31	STORE YOUR OWN GRAIN	D20	2 193 102											
24	"	14	OPERATING LOAN ADVANCE	LN	2 000 0 –					2000 00 –						
25	"	20	F.I.L. TRACTOR	LN	1 000 0 –					1000 00 –						

	TRIAL BALANCE DR	TRIAL BALANCE CR	POSTING DR	POSTING CR
Cash	0.00		85.36	85.36
Bank	2,467.39		234,939.04	215,367.14
Savings	10,400.00			
Grain	60,000.00			
Feed	10,000.00			
Cattle	59,577.00			
Land	180,000.00			
Buildings	85,528.75			
Machinery	58,255.31			
Power Equipment	106,321.18			
Accumulated Capital Cost Allowance		73,849.59		
Investment Tax Credit	4,321.25			
Operating Loan		80,000.00	28,000.00 20,000.00 32,000.00	20,000.00 50,000.00
FIL - Truck		13,275.08	3,953.00	
FIL - Tractor				10,000.00
AFDL - Disc				10,000.00
KEUDF - Loan		168,075.84	3,105.49	
Owner's Equity		241,670.37		
Owner's Contributions				
Owner's Withdrawals				
Machinery Repairs & Maintenance				
Truck Repairs & Maintenance				
Gas, Oil, etc.				
Auto Expenses				
Hardware & Small Tools				
Interest, S/C, etc.				
Feed & Straw				
Freight & Trucking				
Fertilizer				
Cattle Purchases				
Utilities				
Insurance, Licenses, etc.				
Sprays & Other Chemicals				
Salaries & Wages				
Crop Supplies				
Building Rep. & Maint.				
Custom Work				
Cattle Sales				
Wheat Sales				
C.W.B. Payments				
Property Taxes				
Accounting & Legal Fees				
Capital Cost Claimed				
TOTALS	576,870.88	576,870.88	502,391.54	502,391.54

NET FARM INCOME FOR THE YEAR
TOTALS

5) Adjusting Entries

An adjusting entry is an accounting tool which enable you to record transactions when no cheque has been written or no deposit made.

An example of this would be depreciation, a figure which like most adjusting entries, must be calculated. (see section on Capital Cost Allowance for calculating this figure)

Double entry rules apply for making these entries, one account must be credited and another debited. And usually, both a balance sheet and an income statement account are affected.

The amount of Capital Cost Allowance being claimed by South farms is $32,707.42. This amount must be claimed as an expense for tax purposes, and added to the amount of depreciation already claimed until now.

It would be entered in the following way:

	TRIAL BALANCE		POSTINGS		ADJUSTING ENTRIES	
	DR	CR	DR	CR	DR	CR
Accumulated Capital cost		73,849.59				32,707.42
Capital Cost Claimed					32,707.42	

The rest of the adjusting entries for South Farms are:

		DEBIT	CREDIT
1.	Owner's Withdrawal	232.79	
	Auto Expense		232.79
	To charge 1/3 of car expense to personal to satisfy the tax guidelines (1/3 x 698.38)		
2.	Investment Tax Credit	5,210.51	
	Machinery		1,439.51
	Power Equipment		3,780.00
	To record investment tax credit for the new fixed assets purchased ($4,000 x .07, 20,000 x .07, 435.79 x .07)		

6) Sort Account Balances

The adjusted account balances must be sorted into columns according to whether they are used in preparing the income statement or balance sheet.

There are two steps involved:

1) Calculate the final balance in each account. To do this, combine Debit and Credit amounts across the page and calculate the final total. Now, Debits can be added to Debits, and Credits to Credits, but not Debits to Credits.

   Add all the Debit entries; add all the Credit entries. If there are more Debits than Credits, the final balance is a Debit or if the Credits win out the final balance is a Credit.

   The following example might make this clearer:

	TRIAL BALANCE		POSTINGS		BALANCE SHEET	
	DR	CR	DR	CR	DR	CR
BANK	2467.39		234,939.04	215,367.14	22,039.29	

2) Sort the final balance into either the 'Income Statement' or 'Balance Sheet' columns. Remember:

   - Revenue and expenses appear on the Income Statement
   - Assets, liabilities and owners equity are on the balance sheet.

7) Calculate Net Income

Total the Income Statement and Balance Sheet columns. The difference between the Debit and Credit totals of the Income Statement columns is the net income or loss.

Balance the Balance Sheet columns by adding the net income or loss. This is a proof of the accuracy with which the work sheet has been prepared.

Below is the completed work sheet.

SOUTH FARMS
WORK SHEET

	TRIAL BALANCE		POSTING		ADJUSTING ENTRIES		INCOME STATEMENT		BALANCE SHEET	
	DR	CR	DR	CR	DR	CR	DR	CR	DR	CR
Cash	0.00								0.00	
Bank	2,467.39		85.36	85.36					22,039.29	
Savings	10,400.00		234,939.04	215,367.14					12,900.00	
Grain	60,000.00		2,500.00						60,000.00	
Feed	10,000.00								10,000.00	
Cattle	59,577.00								59,577.00	
Land	180,000.00								180,000.00	
Buildings	85,528.75								85,528.75	
Machinery	58,255.31		435.79							
Power Equipment	106,321.18		20,000.00	10,000.00		2) 1,430.51			67,260.59	
Accumulated Capital Cost Allowance		73,849.59	54,000.00	42,000.00		2) 3,780.00			114,541.18	
Investment Tax Credit	4,321.25				5,210.51(2	3)32,707.42				106,557.01
Operating Loan		80,000.00	28,000.00						9,531.76	
FIL - Truck		13,275.08	20,000.00	20,000.00						70,000.00
FIL - Tractor			32,000.00	50,000.00						9,322.08
AFDL - Disc			3,953.00							10,000.00
KEUDF - Loan		168,075.84	3,105.49	10,000.00						10,000.00
Owner's Equity		241,670.37		10,000.00						164,970.35
Owner's Contributions										241,670.37
Owner's Withdrawals				58.96						58.96
Machinery Repairs & Maintenance			3,257.41		232.79(1				3,490.20	
Truck Repairs & Maintenance			3,880.48				3,880.48			
Gas, Oil, etc.			1,264.32				1,264.32			
Auto Expenses			2,568.14				2,568.14			
Hardware & Small Tools			698.38			1) 232.79	465.59			
Interest, S/C, etc.			88.97				88.97			
Feed & Straw			18,705.09				18,705.09			
Freight & Trucking			2,478.00				2,478.00			
Fertilizer			513.00				513.00			
Cattle Purchases			10,000.00				10,000.00			
Utilities			54,258.00				54,258.00			
Insurance, Licenses, etc.			26.00				26.00			
Sprays & Other Chemicals			528.00				528.00			
Salaries & Wages			1,500.00				1,500.00			
Crop Supplies			250.00				250.00			
Building Rep. & Maint.			270.31				270.31			
Custom Work			853.76				853.76			
Cattle Sales				5,500.00				5,500.00		
Wheat Sales				60,498.27				60,498.27		
C.W.B. Payments				74,684.45				74,684.45		
Property Taxes				4,197.36				4,197.36		
Accounting & Legal Fees			1,433.00				1,433.00			
Capital Cost Claimed			800.00				800.00			
					32,707.42(3		32,707.42			
TOTALS	576,870.88	576,870.88	502,391.54	502,391.54	38,150.72	38,150.72	132,590.08	144,880.08	624,868.77	612,578.77
NET FARM INCOME FOR THE YEAR							12,290.00			12,290.00
TOTALS							144,880.08	144,880.08	624,868.77	624,868.77

FINANCIAL STATEMENTS

Financial statements are the final product of the accounting process and summarize, for interested parties, the financial activity of the business.

The statements, income statement and balance sheet, are prepared from the information on the work sheet. This is the step where Debits and Credits are left behind and the information is put into a standard format which users of the information should understand.

INCOME STATEMENTS

This statement summarizes the revenue and expenses of the business during the fiscal year. This statement, which can also be called a "Profit and Loss" statement show the performance of the business.

The format of the statement is as follows:

NAME OF BUSINESS
INCOME STATEMENT

REVENUES			
_____		$ _____	
_____		$ _____	
_____		$ _____	
_____		$ _____	
	TOTAL REVENUES		$ _____
EXPENSES			
_____		$ _____	
_____		$ _____	
_____		$ _____	
_____		$ _____	
	TOTAL EXPENSES		$ _____
NET INCOME			$ _____

CASH & ACCURAL METHODS OF ACCOUNTING

There are two ways of reporting income for tax purposes.

CASH METHOD Only revenue that is actually received is reported as income, and only expenses that are actually paid are shown as tax expenses.

ACCRUAL METHOD Income is reported in the year that it is earned, regardless of when payment is received. Expenses are deducted in the year in which they are incurred, whether actual payment has been made or not.

Most farm tax returns are prepared on a cash basis, which allows a certain degree of manipulation for tax purposes.

However, the cash method may not fully reflect the farms actual income and expenses for the year because:

- some of the sales may represent production from a previous year
- not all of the years production may be sold during the year
- items purchased for next years production are entered as this years expense.

So to measure the actual productivity of your farm business, a cash income statement isn't that useful.

An accrual income statement matches income and corresponding expenses to the same fiscal period so that you can determine actual productivity.

By using beginning and ending inventories, adjustments can be made to a cash income statement so that income reflects production for the year rather than total sales.

EXAMPLE

SOUTH FARMS

NET FARM INCOME (Tax or Cash Basis)	$ 12,290
ADD: ENDING INVENTORY	$255,000
LESS: BEGINNING INVENTORY	$220,000
NET FARM INCOME (Management or Accrual Basis)	$ 47,290

BALANCE SHEET

A balance sheet shows the financial position of a business at a particular point in time. Listed on this statement are the assets, liabilities and owner's equity of the business, using the following format.

SOUTH FARMS
BALANCE SHEET
As At December 31, 1982

ASSETS

Current Assets:		
-	$	
-		
-		
-		
-		
-		
Total Current Assets		$
Fixed Assets		
-	$	
-		
-		
-		
Less: Accumulated C.C.A.		
Investment Tax Credit		
Net Fixed Assets		$
TOTAL ASSETS		$

LIABILITIES AND OWNER'S EQUITY

Current Liabilities		
-	$	
Total Current Liabilties	$	
Long Term Liabilities	$	
-		
-		
-		
-		
Less: Current Portion Long Term Debt	$	
Total Long Term Liabilities	$	
TOTAL LIABILITIES		$

OWNER'S EQUITY

Retained Earnings Jan 1.	$	
Add: Owner's Contribution		
Less: Owner's Withdrawal		
Add: Net Farm Income		
Retained Earnings Dec 31	$	
TOTAL LIABILITIES AND OWNERS EQUITY		$

Statement No.1

SOUTH FARMS
STATEMENT OF FARM INCOME FOR
THE YEAR ENDED DECEMBER 31, 1982

INCOME		
Wheat Sales	$ 74,684.45	
Cattle Sales	60,498.27	
Custom Work	5,500.00	
Canadian Wheat Board Payments	4,197.36	
Total Income		$144,880.08
DEDUCT EXPENSES		
Repairs & Maintenance - Machinery	$ 3,880.48	
- Truck	1,264.32	
- Buildings	853.76	
Gas, Oil, etc.	2,568.14	
Auto Expenses	465.59	
Hardware & Small Tools	88.97	
Interest, Service Charges etc.	18,705.09	
Feed & Straw	2,478.00	
Freight & Trucking	513.00	
Fertilizer	10,000.00	
Cattle Purchases	54,258.00	
Utilities	26.00	
Insurance, Licenses, etc.	528.00	
Sprays & Other Chemicals	1,500.00	
Salaries & Wages	250.00	
Crop Supplies	270.31	
Property Taxes	1,433.00	
Accounting & Legal Fees	800.00	
Capital Cost Claimed	32,707.42	
Total Expenses		$132,590.08
NET FARM INCOME FOR THE YEAR		$ 12,290.00

SOUTH FARMS
STATEMENT OF FINANCIAL POSITION
as at December 31, 1982
(BALANCE SHEET)

ASSETS				
Current Assets:				
Bank			$ 22,039.29	
Savings			12,900.00	
Grain			60,000.00	
Feed			10,000.00	
Cattle			59,577.00	
Total Current Assets				$164,516.29
Fixed Assets:				
Land			$180,000.00	
Buildings	$ 85,528.75			
Machinery	67,260.59			
Power Equipment	114,541.18	$267,330.52		
Less: Accumulated CCA		106,557.01	$160,773.51	
Investment Tax Credit			9,531.76	
Net Fixed Assets				$350,305.27
TOTAL ASSETS				$514,821.56
LIABILITIES AND OWNER'S EQUITY				
Current Liabilities:				
Operating Loan			$ 70,000.00	
Current Portion - Long-term debt			10,803.94	
Total Current Liabilities				$ 80,803.94
Long-Term Liabilities				
FIL - Truck		$ 9,322.08		
FIL - Tractor		10,000.00		
AFDL - Disc		10,000.00		
KEUDF - Land Loan		164,970.35	$194,292.43	
Less: Current Portion - Long-Term Debt			10,803.94	
Total Long-Term Liabilities				$183,488.49
TOTAL LIABILITIES				$264,292.43
OWNER'S EQUITY				
Retained Earnings January 1	$241,670.37			
Add: Owner's Contribution	58.96	$241,729.33		
Less: Owner's Withdrawals		3,490.20	$238,239.13	
Add: Net Farm Income			12,290,00	
Retained Earnings December 31				$250,529.13
TOTAL LIABILITIES AND OWNER'S EQUITY				$514,821.56

PAYROLL RECORDS

Years ago, keeping track of how much you owed an employee for the time he worked for you was a simple task. You multiplied the time he worked by the rate of pay and paid him that amount.

Nowadays, things aren't that simple because you must hold back and remit part of your employee's pay directly to the government to cover Income Taxes, Canada Pension Plan and Unemployment Insurance. As well, you as an employer have to make some corresponding contributions.

You need to keep track of the deductions and contributions you make, as well as the net and gross amounts of your employee's pay through payroll records.

If you have never employed someone before, but are about to start, there are several things you need to do.

1) Contact - Revenue Canada
   220 4th Avenue S.E.
   Calgary, Alberta
   Phone: 2314225

2) Ask for an Employer Number. They will assign this over the phone and send you a form you must fill out and return to them. This means you are registered with them as an employer.

3) You will also be sent a form called a TD-20 which you must get your prospective employee to fill out. This form, which you keep, will indicate what tax bracket your employee will be in and helps you determine what tax deductions to make.

4) Revenue Canada will also send you tables which you can use in calculating the necessary deductions for Canada Pension, Income Tax and Unemployment Insurance.

5) Every employer is required by law to remit the above deductions to Revenue Canada along with the employer contributions no later than the 15th day of the month following the month in which the employee was paid. Once you are registered as an employer, Revenue Canada will send you a form every month which you return to them when you make your remittances. These can be paid through the mail or at any bank.

Whether you purchase a payroll record book, or keep the information in your accounting journal (choose a separate page - leave engouh room for your financial records) you need to have payroll records like the following:

The example below shows a payroll record for 1 employee earning $1,200/month.

NAME OF EMPLOYEE	GROSS PAY	DEDUCTIONS FROM PAY			NET PAY	EMPLOYER'S CONTRIBUTIONS		REMITTANCE TO REVENUE CANADA
		INCOME TAX	CANADA PENSION PLAN	UNEMPLOYMENT INSURANCE		CANADA PENSION	UNEMPLOYMENT INSURANCE	
A. Riley	1200.00	200.00	50.00	45.00	905.00	50.00	63.00	408.00

SPOUSAL SALARIES

When paying a spouse a wage or salary, keep the following points in mind.

- The amount paid must be reasonable, given the type of work done.
- Records should be kept indicating the type and amount of work done.
- Canada Pension and Income Tax must be deducted.
- No Unemployment Insurance deductions are necessary.

CAPITAL COST ALLOWANCE

Capital assets are those which have a useful life longer than one year, such as machinery, buildings and equipment. With few exceptions, purchases of a capital nature may not be deducted in full when computing income for tax purposes for the year the purchase was made. Instead, a portion of the capital expense is deducted from income over several years. This portion is called Capital Cost Allowance.

Calculating Capital Cost Allowance

The calculation involved in determining capital cost allowance for the year is not complicated. It has changed to some extent since November,1981 when the tax rules for determining the C.C.A. of new assets was changed to allow only ½ the normal C.C.A. in the first year.

The following example shows how to calculate the C.C.A. for Class 10 assets. During the year a new tractor was purchased for $50,000. The Investment Tax Credit is $3500. An older tractor was sold for $15,000.

1) Take the undepreciated capital cost of assets at the beginning of the year,	$150,000
2) Add the cost of additions during the year (less any investment tax credit available) $50,000-$3500= $46,500	$46,500
3) Deduct the proceeds of any disposals (up to the original cost)	$15,000
	$181,500
4) Apply the C.C.A. rate to the remaining balance. $181,500 X .30	$54,450
5) Deduct the adjustment for new assets. ½ X 46,500 X .30	$6,975
Maximum C.C.A. deduction	$47,475
Undepreciated capital cost at year end. $181,500 - $47,475=	$134,025

SOUTH FARMS

SCHEDULE OF FIXED ASSETS AND CAPITAL COST
CLAIMED AS AT DECEMBER 31, 1982

	Class 6 10%	Class 8 20%	Class 10 30%	TOTAL
Undepreciated Capital Cost December 31, 1981	55,528.75	38,255.31	82,471.59	176,255.65
Additions:				
Air Compressor		405.28		405.28
Disc		18,600.00		18,600.00
Tractor			50,220.00	50,220.00
	55,528.75	57,260.59	132,691.59	245,480.93
Less: Disposals				
Disc		10,000.00		10,000.00
Tractor			42,000.00	42,000.00
	55,528.75	47,260.59	90,691.59	193,480.93
Less: 1/2 of Net Purchases		4,502.64	4,110.00	8,612.64
Capital Cost Claimed	55,528.75	42,757.95	86,581.59	184,868.29
	5,552.88	8,551.59	18,602.95	32,707.42
Add: 1/2 of Net Purchases	49,975.87	34,206.36	67,978.64	152,160.87
		4,502.64	4,110.00	8,612.64
Undepreciated Capital Cost December 31, 1982	49,975.87	38,709.00	72,088.64	160,773.51

A good rule of thumb: Claim the required amount of capital cost allowance first against the classes with the lowest capital cost allowance rates, leaving the greatest amount available for future years in the higher rate classes. (Tax Principles to Remember)

WORKSHEET NO. 1

PROJECTED FARM INCOME & EXPENSES FOR TAX PLANNING

	Amount to Date	Projected for Balance of Year	Total Expected for the Year
Income:			
Crops & Seeds			
Fruit			
Vegetables			
Grain			
Other			
C.W.B. Payment & Cash Advance			
Forage Crops			
Livestock - Beef			
- Swine			
- Other			
Dairy Products			
Poultry Products			
Other farm income,			
Income Assurance			
Interest Rebate, etc.			
Other			
Gross Income			
Expenses:			
Salaries, wages, C.P.P., U.I.C.			
Rent			
Interest			
Property Taxes & Insurance			
Fuel & Lubricants			
Repair & Maintenance			
Livestock Purchase			
Vet, medicine & breeding fee			
Fertilizer sprays & chemicals			
Feed and straw			
Plants & seeds			
Custom work			
Repayment of C.W.B. Advance			
Utilities			
Land Clearing or Improving			
Legal and accounting			
Other expenses			
Capital Cost Allowance			
Total Expenses			
Projected Net Farm Income			

WORKSHEET NO. 2

ESTIMATE OF INCOME TAX PAYABLE

		Projected Year's Total
Net Farm Income (From Worksheet 1)	(1)	_____
Minus: Livestock Inventory Sales (last year)	(2)	_____
Add: Livestock Inventory Sales (this year)	(3)	_____
Taxable Net Farm Income	(4)	_____
Add: Taxable Capital Gains	(5)	_____
Taxable Non-Farm Income	(6)	_____
Total Taxable Income Before Deductions	(7)	_____
Less Deductions: C.P.P. Contributions	(8)	_____
R.R.S.P. Contributions	(9)	_____
Personal exemptions	(10)	_____
Other Deductions	(11)	_____
Total Deductions	(12)	_____
Taxable Income (7) - (12)		_____
Estimated Income Tax Payable	(13)	_____
Less Tax Credits: Investment Tax Credit) Dividend Tax Credit) Employment Tax Credit)	(14)	_____
Estimated Tax Due (13) - (14)		_____

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INCOME TAX

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* TAX TREATMENT OF TREE FARMERS, 1977
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FARM ESTATE PLANNING, JANUARY 1984, REV. (IN PREP.)
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PRINCIPLES OF LAW FOR RURAL ALBERTA, UNIVERSITY OF ALBERTA 1981 - TEMPORARILY OUT OF PRINT.

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A FIRST LOOK AT FARM COMPUTERS, AGRIFAX OCTOBER 1979 (FS818-7)
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* COMPU-FARM MONTHLY NEWSLETTER
HOW TO SELECT THE RIGHT FARM ACCOUNTING SOFTWARE, JANUARY 1984 (AGDEX 818-22)

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* PRAIRIE PROVINCES FARM ACCOUNT BOOK (AGDEX 818-1)
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