Banking Fundamentals

• a **bank is an institution that accepts customer deposits and offers loans to individuals and corporate clients.**

• Banks **make money by charging higher interest on loans than the interest they pay on customer deposits.**

Banking fundamentals refer to the concepts and principles relating to the practice of banking. Banking is an industry that deals with credit facilities, storage for cash, investments, and other financial transactions. The banking industry is one of the key drivers of most economies because it channels funds to borrowers with productive investments.

Banks perform a myriad of functions, including deposits and withdrawals, currency exchange, forex trading, and wealth management. Also, they act as a link between depositors and borrowers, and they use the funds deposited by their customers to provide credit facilities to people who want to borrow.

Banks make money by charging an interest rate on loans, where they profit by charging a higher interest rate than the interest rate they pay on customer deposits. However, they must comply with the regulations set by the central bank or national government.

How Banking Industry Works

In Kenya, banks are regulated by the CBK. Banks must retain at least 10% of each deposit on hand but can lend out the other 90% as loans. The reserve requirement applies to all types of banks that are licensed to operate in the Kenya, and they can hold the reserve as a deposit in the local Central bank or as cash in the vault.

Banking Fundamentals – Types of Bank Accounts

The common types of bank accounts include:

1. Savings account

A savings account is a bank account that a customer can deposit money in that they do not need right away, but that is available for withdrawal whenever needed. The bank loans out the money to borrowers and charges interest on the amount of credit disbursed.

2. Checking account

A checking account allows customers to access their deposited funds with ease, and they can use it to make their financial transactions such as paying bills. A customer can access the funds by writing a check, using a debit card to withdraw money or make payments, or by setting up automatic transfers to another account.

3. Certificate of deposit

A certificate of deposit is a bank account that holds a fixed amount of money for a defined period of time such as six months, one year, two years, etc. It pays a fixed interest rate on the amount held.

Types of Banks

When you think of a bank, the first thing that comes to mind might be the institution that holds your checking or savings account. But there are several different types of banks, all serving different needs.

You might not have heard of all of these banks, but each example probably plays some part in your everyday life. Different banks specialize in distinct areas, which makes sense—you want your local bank to put everything they can into serving you and your community. Likewise, online banks can do their thing without the overhead of managing multiple branch locations.

Some of the most common banks are listed below, but the dividing lines are not always clear.

- **Retail banks** are probably the banks you're most familiar with. Your checking and savings accounts are often kept with a retail bank, which focuses on consumers (or the general public) as customers. These banks offer loans and may provide credit cards, and they're the ones with numerous branch locations in populated areas.1

- **Commercial banks** focus on business customers. Businesses need checking accounts just like individuals do. But they also need complex services, and the dollar amounts (and the number of transactions) can be substantial. Commercial banks, which are also called business banks or corporate banks, manage payments for customers, provide lines of credit to manage cash flow, and offer foreign exchange services for companies that do business overseas.2
- **Investment banks** help businesses raise capital in financial markets. If a company wants to go public or sell debt to investors, it often uses an investment bank. This kind of bank also may advise corporations on mergers and acquisitions.1
- **Private banks** provide services exclusively to wealthy clients, usually those with at least $1 million of net worth. They help clients manage their wealth, provide tax advice, and set up trusts to avoid taxes when leaving money to descendants.1
- **Central banks** manage the monetary system for a government. For example, the Federal Reserve is the U.S. central bank responsible for supervising banks and setting monetary policy to control inflation, reduce unemployment, and provide for moderate lending rates.3
- **Credit unions** are similar to banks, but they are not-for-profit organizations owned by their customers. (Investors own most banks.) Credit unions offer products and services more or less identical to retail banks. The main difference is that credit union members share some characteristic in common—where they live, their occupation, or an organization they belong to, for example.4
- **Online banks** operate entirely online; there are no physical branch locations available to visit with a teller or personal banker. Many brick-and-mortar banks also offer online services, such as the ability to view accounts and pay bills online, but internet-only banks are different. Internet banks often offer competitive rates on savings accounts, and they're especially likely to offer free checking.5 6
- **Mutual banks** are similar to credit unions because they are owned by members (or customers) instead of outside investors. Also like credit unions, they tend to be active in only a single community.7
- **Savings and loans** are less prevalent than they used to be, but they are still important. This type of bank helped make homeownership mainstream, using savings deposits from customers to fund home loans.8 The name savings and loan is derived from that core activity.

Non-Bank Lenders

Non-bank lenders are increasingly popular sources for loans. Technically, they're not banks, but your experience as a borrower might be similar. You apply for a loan and repay it as if you were working with a bank.

For consumers shopping for loans, non-bank lenders are often attractive. They may use different approval criteria than traditional banks, and rates are often competitive.10 Peer-to-peer lenders are just one example of these marketplace lenders, and they can be an option whether you have high credit scores or you have fair credit.11

Online lenders gained momentum with personal loans, but they offer other products as well. You can borrow for education, a home purchase or refinancing, and more

ACCOUNTING CIRCLE

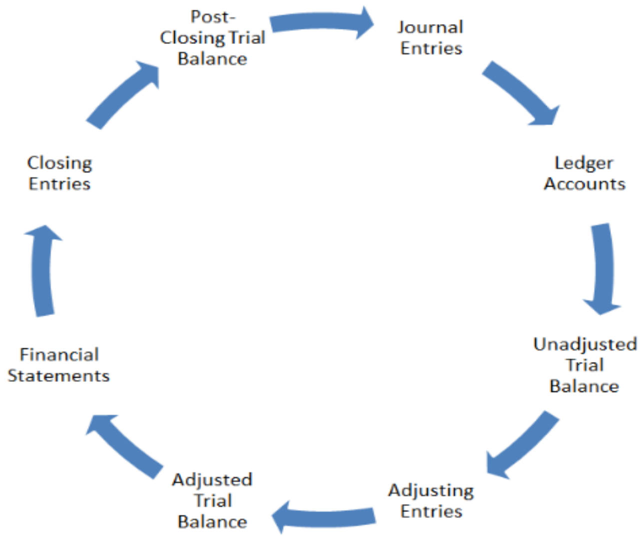
Accounting cycle is a step-by-step process of recording, classification and summarization of economic transactions of a business. It generates useful financial information in the form of financial statements including income statement, balance sheet, cash flow statement and statement of changes in equity.

The time period principle requires that a business should prepare its financial statements on periodic basis. Therefore accounting cycle is followed once during each accounting period. Accounting Cycle starts from the recording of individual transactions and ends on the preparation of financial statements and closing entries.

Major Steps in Accounting Cycle

Following are the major steps involved in the accounting cycle. We will use a simple example problem to explain each step.

1. Analyzing and recording transactions via journal entries
2. Posting journal entries to ledger accounts
3. Preparing unadjusted trial balance
4. Preparing adjusting entries at the end of the period
5. Preparing adjusted trial balance
6. Preparing financial statements
7. Closing temporary accounts via closing entries
8. Preparing post-closing trial balance



The accounting cycle is the holistic process of recording and processing all financial transactions of a company, from when the transaction occurs, to its representation on the financial statements, to closing the accounts. One of the main duties of a bookkeeper is to keep track of the full accounting cycle from start to finish. The cycle repeats itself every fiscal year as long as a company remains in business.

The accounting cycle incorporates all the accounts, journal entries, T accounts, debits, and credits, adjusting entries over a full cycle.

Key Points

- The accounting cycle has 8 Steps.
- Each transaction must be analyzed to determine whether it qualifies as a business transaction.
- The accounting cycle runs within the accounting period.
- The goal of the accounting cycle is to produce financial statements for the company.

Key Terms

- **bookkeeping**: The skill or practice of keeping books or systematic records of financial transactions, e.g., income and expenses.
- **source**: The person, place or thing from which something (information, goods, etc.) comes or is acquired.
- **summarize**: To give a recapitulation of the salient facts; to recapitulate or review

The Accounting Cycle

The accounting cycle is a series of steps performed during the accounting period (some throughout the period and some at the end) to analyze, record, classify, summarize, and report useful financial information for the purpose of preparing financial statements. In bookkeeping, the accounting period is the period for which the books are balanced and the financial statements are prepared. Generally, the accounting period consists of 12 months. However, the beginning of the accounting period differs according to the company. For example, one company may use the regular calendar year, January to December, as the accounting year, while another entity may follow April to March as the accounting period.

Eight Steps in the Accounting Cycle

There are eight steps in the accounting cycle and they are as follows:

- Analyze transactions by examining source documents.
- Journalize transactions in the journal.
- Post journal entries to the accounts in the ledger.
- Prepare a trial balance of the accounts and complete the worksheet (includes adjusting entries).
- Prepare financial statements.
- Journalize and post adjusting entries.
- Journalize and post closing entries.
- Prepare a post-closing trial balance.

Source Documents

To begin the accounting cycle, it is necessary to understand what constitutes a business transaction. Business transactions are measurable events that affect the financial condition of a business. Business transactions can be the exchange of goods for cash between the business and an external party, such as the sale of a book, or they can involve paying salaries to employees. These events have one fundamental thing in common: they have caused a measurable change in the amounts in the accounting equation, assets = liabilities + stockholders’ equity. The evidence that a business event has occurred is a source document. Sales tickets, checks, and invoices are common source documents. Source documents are important because they are the ultimate proof that a business transaction has taken place.

After determining, via the source documents, that an event is a business transaction, it is then entered into the company books via a journal entry. After all the transactions for the period have been entered into the appropriate journals, the journals are posted to the general ledger. The trial balance proves that the books are in balance or that the debits equal the credits. From the trial balance, a company can prepare their financial statements. After the financials are prepared, the month end adjusting and closing entries are recorded (journalized) and posted to the appropriate accounts. After those entries are made, a post-closing trial balance is run. The post-closing trial balance verifies the debits equal the credits and that all beginning balances for permanent accounts are in place.

Steps in the Accounting Cycle

1 Transactions

Transactions: Financial transactions start the process. If there were no financial transactions, there would be nothing to keep track of. Transactions may include a debt payoff, any purchases or acquisition of assets, sales revenue, or any expenses incurred.

Events are analyzed to find the impact on the financial position or to be more specific the impacts on the accounting equation.

Documents such as; a receipt, an invoice, a depreciation schedule, and a bank statement, etc. provide evidence that an economic event has actually occurred.

The Main difference between transaction and event is when an event brings change to account balances, it is classified as a transaction and recorded in the books.

Difference between Event and Transaction

Event	Transaction
(1) All events are not transactions.	(1) All transactions are events.
(2) An event may or may not bring change in the financial position of a person, family, or organization.	(2) An event must bring financial change.
(3) Financial changes caused by events may or may not be measurable in terms of money. For example, the death of a skilled employee may bring heavy loss to a business, but this loss is not measurable in terms of money.	(3) The financial changes caused by transactions must be measurable in terms of money.

(4) Events are used in a wider sense. It may or may not require two parties for the occurrence of an event.	(4) Transactions are used comparatively in a narrow sense. In the case of transaction two parties are must.
(5) Transfer of goods or services may or may not occur for an event.	(5) As a consequence of transactions transfer of goods or service is a must. Of course, in some cases, there is an exception. For example, burning of goods, fixed asset depreciation etc.
(6) It is. not necessary that every event will be recorded in the books of accounts. It is needless to record any event in the books of accounts if it is not measurable in terms of money.	(6) Every transaction must be recorded in the books of accounts; otherwise accurate results cannot be ascertained from the books of accounts.
(7) Transaction relating event is settled for cash.	(7) Financial transactions may be settled in Cash or are made on credit.
(8) As per accounting principle of events— (a) Cash statement. (b) Separate statements for receipts and payments head wise and, (c) Final statement of receipts and payments are made.	(8) In the accounting process of the transaction in the first phase journalizing, in the second phase posting in the ledger and in the third phase financial statement is prepared.
(9) The scope of the event is very wide.	(9) The scope of the transaction is limited.
(10) The scope of the event is very wide.	(10) The scope of the transaction is limited.
(11) Transactions related to events are not always supported by evidence.	(11) Business transactions must be supported by evidence.

So you can say that Transactions are events that;

(i) cause an immediate change in the financial resources or obligations of the business.
(ii) can be measured objectively in monetary terms.

2 Journal Entries

Transactions having an impact on the financial position of a business are recorded in the general journal.

Journal Entries: With the transactions set in place, the next step is to record these entries in the company's journal in chronological order. In debiting one or more accounts and crediting one or more accounts, the debits and credits must always balance.

7 types of journal books are maintained in accounting for the convenient keeping of accounts and recording transactions of similar nature.

7 types of journal books are maintained in accounting for the convenient keeping of accounts and recording transactions of similar nature.

Under the double-entry system, there are mainly 7 different types of journal in accounting. Transactions are primarily recorded in the journal and thereafter posted to the ledger.

It is difficult to find out effects and information relating to the transaction if all the transactions are recorded in a single journal.

Recording of all transactions in one general journal is a time consuming, laborious and troublesome task.

That is why in modem times the use of many journals instead of one journal has been introduced in almost all business concerns, especially the medium and large size business concerns.

For convenient keeping of accounts, maintaining more than one special journal according to the nature of transactions instead of one journal is called classification of the journal.

The transactions of the same nature are recorded in a special journal. These are termed as a daily journal, subsidiary journal or special journal.

Most large size business concerns record particular transactions in special journal, side by side general journal.

Types of Journal in Accounting

1. Purchase journal
2. Sales journal
3. Cash receipts journal
4. Cash payment/disbursement journal
5. Purchase return journal
6. Sales return journal
7. Journal proper/General journal

Here it should be mentioned that most of the business organizations of our country are of small or medium size. These organizations maintain cash book for recording daily cash receipts and cash payments instead of maintaining cash receipt journal and cash payment journal separately.

But where cash receipts journal and cash payments journal are maintained cash book is not needed.

Purchase Journal

The special journal used for recording the credit purchase of merchandise is called a purchase journal.

In purchase journal transactions of merchandise purchased on credit for sale are recorded. An asset purchased on the account is not recorded in the purchase journal.

But many are of the opinion to record all credit transactions in the multi-column purchase journal.

For instance, Pyle and Larson have shown credit purchase of assets and supplies, etc. in a purchase journal under a separate column – debiting asset or office supplies and crediting accounts payable.

Since purchase journal is meant for recording merchandise purchased on credit purchase of assets and other things on credit should not be recorded in the purchase journal rather a recording of these in general journal is more acceptable.

The format of the purchase journal:

Single-column purchase journal:

Purchase Journal

Date	Accounts credited	Terms	Reference	Purchase/Inventory Dr. Accounts Payable Cr.

A single-column purchase journal is used only for recording credit purchase of merchandise. In this respect, the format of the purchase journal under periodic and perpetual systems is the same.

But in the case of periodic system purchase account and in the case of the perpetual system merchandise inventory accounts are debited and account payable is credited in both the cases:

Multi-column purchase journal

Purchase Journal
(Multi-column)

Date	Accounts credited	Terms	Ref.	Accounts Payable Cr.	Purchase / Inventory Dr.	Supplies Dr.	Other Accounts Dr.

Some organizations use a multi-column purchase journal wherein credit purchase of merchandise, assets and other things are recorded. Organizations concerned use columns of the journal according to their needs.

Trade discount

At the time of sale, the value which is exempted from catalog price as per terms by the seller to the purchaser is called trade discount.

The trade discount is allowed in order to give benefit to the buyer of goods so that he can earn a definite amount of profit by selling goods. For example, at the time of price fixing the price of a commodity is fixed at $100 including a 5% trade discount.

At the time of selling the seller can sell this commodity granting a 5% trade discount i.e. the buyer gets the benefit to sell the commodity at $95. Trade discount is not recorded in the books of account because it does not bring any financial change of seller or buyer.

Only in the invoice, the trade discount is shown by way of deduction from the invoice price. In purchase and sale books/journals the net purchase or sale value after deducting trade discount from the total value of goods is shown.

In both, cases i.e. in cash sale or credit sale trade discount is generally allowed.

Posting in Ledger

The purchase journal is not written in accordance with a double-entry system i.e., it is not written determining the debit account and credit account.

So, at the time of posting in the ledger, its dual aspects are to be completed. It is not mandatory to show the journal entry which is submitted at the end of the purchase journal.

For convenient postings in the ledger, these journals have been given. Opening purchase account in the ledger the weekly or monthly purchase is to be debited from the miscellaneous account in its debit side.

Opening an individual account in the name of creditor or creditors recorded in the purchase journal respective receivable amounts are credited to the credit side.

Balancing ledger accounts is not generally determined or shown until the end of the year, because posting in these accounts may be needed throughout the whole year.

Sales Journal

Sales journal is used for recording the credit sale of merchandise only.

Cash sale of merchandise is recorded in the cash receipt journal. A credit sale of an asset is recorded in general journal.

Cash Receipts Journal

The special journal used for recording all types of cash receipts is called the cash receipts journal.

In modem age, the introduction of cash receipts journal is in practice in medium and large size business organizations.

All kinds, of cash receipts, are recorded in this journal. The main sources of cash receipts are two; Cash from cash sale and cash from accounts receivable.

There might have other sources of cash receipts. For example, taking a loan from a bank, interest receipts, the cash sale of assets, etc.

Since the cash book does not contain a separate required column for recording cash receipts, it fails to provide information regarding various cash receipts and cash flow.

To overcome these entire limitations multi-column cash receipts journal is required.

Generally in the cash receipts journal to debit columns for cash receipts and cash discount and three credit columns for accounts receivable, sales and other accounts are there. Cash received from various sources other than cash sales and account receivables are recorded in other accounts column.

If the perpetual inventory system is followed in recording merchandise inventory, a separate journal entry is passed along with a sale journal where the cost of goods sold is debited and merchandise inventory is credited.

It may be mentioned that under the periodic inventory system this additional journal entry is not required.

Periodic Inventory System: Under periodic inventory system the format of cash receipt journal is as follows:

Perpetual Inventory System: Under the perpetual inventory system the format of cash receipt journal is as follows:

Cash Receipt Journal

Date	Accounts credited	Ref.	Cash Dr.	Sales Discount Dr.	Accounts receivable Cr.	Sales Cr.	Other accounts Cr.	Cost of goods sold Dr Merchandise Inventory Cr.

Cash Payment Journal

The; special journal used for recording various transactions relating to cash payment is called a cash payment journal. Business concerns usually pay debts by cheques.

Payment by cheque is treated as a cash payment.

For the acceptability of cash payment, business organizations pay bills by cheques. The cash payment journal contains many money columns as cash payments are made under many heads.

Payment to accounts payable is an important item among the cash payment items and for this account payable provision for a separate debit, the money column is made in cash payment journal.

As purchase discount arises with various payments a separate purchase discount credit money column is kept in it. A cash credit column is provided for cash payment and cheque payment.

Another debit column for office supplies is also contained in the cash payment journal. Besides, for showing other payment there contains another accounts-debit column. A format of the multi-column cash payments journal is shown below:

Cash Payment Journal

Date	Accounts debited	Ref.	Other accounts Dr.	Accounts payable Dr.	Purch-ase Dr.	Purchase discount Cr.	Cash Cr.

Purchase Return Journal

The special journal, where purchase returns of credit purchase are recorded, is called a purchase return journal.

In the case of isolation of purchase agreement or in the case of defective goods the purchaser returns the- goods to the seller. While returning goods to the seller a slip containing reasons for the return of goods is sent along with goods.

This is called a debit note. The seller also sends a note to the purchaser as a reply which is called a credit note. It may be mentioned that goods purchased on cash if returned are not recorded in the purchase return journal.

A format of purchase return journal is shown below:

Purchase Return Journal

Date	Accounts debited	Terms	Ref.	Debit note	Accounts payable Purchase return	Dr Cr

Sales Return Journal

The special journal, where the credit sale returns are recorded, is called a sales return journal. The sales return journal is prepared from debit notes sent by the buyer with returned goods. In reply, the seller sends a credit note.

The format of sales return is similar to that of sales journal excepting challan/invoice column where credit note is written.

It may be mentioned that where the sales return transactions are large in number this sales return journal is maintained.

But where such return transactions are very few in number, these are recorded in the general journal.

Journal Proper

The transactions other than the transactions recorded in cash receipts journal, cash payment special, purchase journal, sales journal, etc. are recorded in journal proper or general journal.

For example;

Purchase of assets on credit, the stock of goods at the year-end, rectification of errors, adjustment of accounts, etc. are recorded in journal proper.

Therefore, the journal, wherein the transactions which cannot be directly recorded in a particular journal are recorded, is called journal proper.

In the journal proper generally, the following transaction is recorded;

1. **Opening Entry:** The journal entry which is passed at the beginning of the current year for recording assets and liabilities of the previous year is called opening entry.
2. **Closing Entry:** The journal entries, which are passed to close the periodical expenses and income transferring them to the income statement, are called closing entries. That is all income – expense accounts, sales-purchase accounts, and profit- loss accounts are closed through transfer to the income statement.
3. **Adjustment Entry:** The journal entry through which accrued expenses and income and advance income, expenses, depreciation, specific provisions, etc. are adjusted is called adjustment entry.
4. **Rectification Entry:** The entry, through which errors in accounts are rectified, is called rectification entry.

5. **Transfer Entry:** The entry which is made for transferring fund from one account to another account is called transfer entry.
6. **Credit Purchase and Sale of Assets:** The entry which is needed for recording transactions relating to credit purchase and sale of assets is called credit purchase and sale of assets entry. For example, Furniture purchased from Sonargaon Furniture for $5,000.
7. **Other Entry:** Entries that cannot be recorded in another journal.

3 Posting to the General Ledger (GL)

Posting to the GL: The journal entries are then posted to the general ledger where a summary of all transactions to individual accounts can be seen.

Transactions recorded in the general journal are then posted to the general ledger accounts.

The accounts classify accounting data into certain categories and they are recorded in general journal entries according to that classification.

In accounting, an account is a functional unit, identified by an account number that serves a particular accounting purpose where one person has primary responsibility for it.

An account is an element in an accounting system that is used to classify and summarize measurements of business activity.

Recording of transactions of similar nature relating to income, expenditure, assets, and liabilities at the end of an accounting period of a particular business under appropriate heads as per principles and rules of accounting in the condensed and classified statement is called account.

4 Types of Accounts are;

1. Asset account.
2. Liability account.
3. Expenditure account.
4. Income account.

According to the objective and the principle of the accounting equation accounts are four types;

Accounting Equation indicates that for every debit there must be an equal credit. assets, liabilities and owners' equity are the three components of it. Accounting equation suggests that for every debit there must be a credit.

Assets, liabilities and owners' equity are the three components of the accounting equation that make up a company's balance sheet

Assets, liabilities and owners' equity are the three components that make up a company's balance sheet. The balance sheet, which shows a business's financial condition at any point, is based on this equation.

This equation is the framework of tracking money as it flows in and out of an economic entity.

Assets

Assets or the economic resources of the entity which is owned by it. Items like; cash, accounts receivable (amounts owed to a firm by its customers), inventories, land, buildings, equipment, and even intangible assets like patents and other legal rights and claims.

Liabilities

Liabilities means claims of creditors which are the amounts of a business entity owed to 3rd parties like; money borrowed from the Lenders or creditors, due wages payment, payable bills, and notes, etc.

Owners' Equity

Owners' equity is known as the owner "interest" in the business. It is also referred to as net assets because it is equivalent to assets minus liabilities

Accounting Equation demonstrates the dual aspect of a transaction and proofs that Debit = Credit. Here is a table to show you the effects of transactions on the accounting equation.

Transaction Type	**Assets**	**Liabilities + Equity**
Buy fixed assets on credit	Fixed assets increase	Accounts payable (liability) increases
Buy inventory on credit	Inventory increases	Accounts payable (liability) increases
Buy inventory on credit	Inventory increases	Accounts payable (liability) increases
Pay dividends	Cash decreases	Retained earnings (equity) decreases

Pay rent	Cash decreases	Income (equity) decreases
Pay supplier invoices	Cash decreases	Accounts payable (liability) decreases
Sell goods on credit (effect 1)	Inventory decreases	Income (equity) decreases
Sell goods on credit (effect 2)	Accounts receivable increases	Income (equity) increases
Sell services on a credit	Accounts receivable increases	Income (equity) increases
Sell stock	Cash increases	Equity Increases

Asset Account

The account kept classifying the transactions for which the assets increase or decrease is called an asset account.

For example, cash account, building account, furniture account, etc.

Liability Account

The account kept classifying the transactions for which liability increases or decreases is called a liability account.

For example, creditors account, loan account, bills payable account, capital account, etc.

Expenditure Account

The account kept under different heads classifying the various expenditures of a business or institution is called an expenditure account.

Income Account

The accounts, kept under different heads having classified die transactions relating to income properly, is called income account.

For example, sale account, interest received account, rent received account, etc.

Besides the above classification according to nature accounts are also classified into the following three types;

1. **Personal account:** The accounts relating to person and organization are personal accounts. For example, Angel Account, Jamuna and Co. Account, etc.
2. **Asset account,** which is discussed earlier.
3. **Nominal or income-expenditure account:** Accounts relating to income, expenditure, and losses are nominal or income-expenditure account. For example, purchase expense account, sales revenue account, salary expense account, rent expense account, etc.

In practice, different formats of accounts are followed.

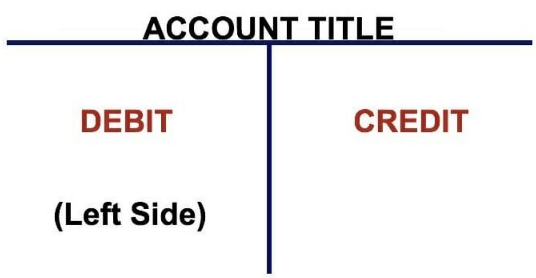
Among them, 'T' form and statement form are popular.

Specimens of both the formats are shown below:

'T' Formats:

The T Account is a visual representation of individual accounts in the form of a "T," making it so that all additions and subtractions (debits and credits) to the account can be easily tracked and represented visually.

Each account will have its own individual T Account, which looks like the following:



Statement Form:

Name of Account : .... **No. : ....**

Date	Account Titles	Folio	Dr.	Cr.	Balance	
					Dr.	Cr.

Understatement form, someone prefers to show balance in one money column instead of showing a debit balance column and credit balance column, as shown in the above format.

4 Trial Balance

Trial Balance: At the end of the accounting period (which may be quarterly, monthly, or yearly, depending on the company), a total balance is calculated for the accounts.

5 Worksheet

Worksheet: When the debits and credits on the trial balance don't match, the bookkeeper must look for errors and make corrective adjustments that are tracked on a worksheet.

6 Adjusting Entries

Adjusting Entries: At the end of the company's accounting period, adjusting entries must be posted to accounts for accruals and deferrals.

7 Financial Statements

Financial Statements: The balance sheet, income statement, and cash flow statement can be prepared using the correct balances.

8 Closing

Closing: The revenue and expense accounts are closed and zeroed out for the next accounting cycle. This is because revenue and expense accounts are income statement accounts, which show performance for a specific period. Balance sheet accounts are not closed because they show the company's financial position at a certain point in time.

General Ledger

The general ledger serves as the eyes and ears of bookkeepers and accountants and shows all financial transactions within a business. Essentially, it is a huge compilation of all transactions recorded on a specific document or in accounting software.

For example, if you want to see the changes in cash levels over the course of the business and all their relevant transactions, you would look at the general ledger, which shows all the debits and credits of cash.