Eezi Accounts

Instruction book

Introduction

EeziAccounts has been specifically designed to be a simple, easy to use accounting package for small businesses, clubs etc. The sections that follow describe how to load and use the program.

Loading the program

1. Insert the CD into it's drive, usually D:
2. The installation will usually begin automatically, if it doesn't then:
3. Click on the Windows START button, then select RUN.
4. In the space provided, type in D:\Setup.exe (or the applicable drive name, maybe E: or F:)
5. Follow the on-screen prompts.

First run

The first time that you run the program you will be asked to fill in your Company details. The information that you enter can later be changed through the "File .... Edit Company Details" menu. The details that you enter here are printed on your reports, invoices and other documents. You will also need to supply other details such as the ruling VAT rate, the date of the start of the financial year, etc.

Changing the currency

You may find that the program is using the wrong currency. This is corrected in the Windows Control Panel by accessing the "Regional Settings". You should choose English - South Africa". The steps are as follows:

1. Close EeziAccounts
2. Click on the Windows START button
3. Slide up to Settings, then across to Control Panel - click on Control Panel
4. Open the Regional Settings item
5. Choose "English – South Africa"
6. Close the Control Panel
7. Restart the computer
8. Open EeziAccounts again

Running more than one company

If you wish to run additional companies you should re-install the program from the CD, but instead of choosing the default Directory and Shortcut locations you should specify a new name that relates to the new company.

Main page view

On the program's main page you can see a summary of the Balance Sheet and the Income Statement:

You cannot enter any data directly into either the Balance Sheet or the Income Statement – this is done through entering transactions, which will be discussed later.

On this screen you also see a row of menu items along the top (File, Accounts, Transactions etc.) as well as a row of icons. The icons carry out some of the most commonly used functions of the program, but all of the program's functions can be carried out through selecting the appropriate menu items.

What follows if a description of what each menu item does. Through these descriptions you will learn how the program works.

File menu items

Save and retrieve backups

When you click on the "save backup of database" menu a screen comes up offering three choices, namely:

1. Quick backup
2. Backup to A: drive (usually stiffy)
3. Backup to a destination of my choice

Explanation of each option

1. The quick backup makes backup copies of the data on the hard drive, in the same folder as the program (usually c:\Program files\EeziAccounts). This means that if the hard drive crashes or the computer goes missing both the main data and the backup will be lost. A common use for this is to make a backup before you begin data entry, especially if you are not too sure that you will do your entries correctly. If you then do make some mistakes and you would like to go back to the position that you were in before you started you can do so using the retrieve facility.

2. Backup to A: is intended to make backup copies to stiffy disks. Check that the disks are in good condition and properly formatted. It is best to change disks between files, especially when the amount of data stored becomes large. When the data files grow too large you will not be able to use this option. In this event you will have to use Microsoft backup, which is part of Windows. Please note that stiffy disks are often not reliable, and you should not rely on them alone for your backups.

3. The last option allows you to backup to other locations such as other folders, network drives, CD writers etc

The "Retrieve backup of database" menu allows you to go back to a previously saved set of data. The choices offered are the same as those for saving. It is important to note that when you retrieve a backup you will lose the current set of data that you were working on.

Backup on existing program

You will note that the program asks if you want to make a quick backup each time it closes. If you say yes this backup will replace any quick backup that you made while working. It is usually a good idea to say yes except where you want to retain your last quick backup.

Compact the databases

After the program has been in use for a long time, especially after many deletions of data or consolidating of statements, the databases become larger than they need to be. Running this utility will simply make the database files smaller where possible; no data will actually be changed or lost.

You are asked if you wish to make a backup before doing the compaction - it is wise to do so.

Load empty databases

 This utility has the effect of deleting all of your data and starting completely afresh. Often users "experiment" with the program after purchase, and would then like to delete all their experiments and start with a clean slate.

WARNING!! This utility will delete all of your data.

Edit company details

This allows you to change the company details that you entered the first time you ran the program. Note that if you call up an old customer statement after making this change the new company details will appear on the statement, not the old ones.

Change financial year start date

When you ran the program for the first time you were asked the date of the first day of the financial year, for example 1 March 2000. This menu option allows you to change that date, and therefore the financial year-end date as well. The date must be entered in the format shown.

Note that all current transactions will still be considered part of the financial year you are working on, despite the transaction dates that were entered.

If you want to close off the financial year and move to the next year, you must use the "End of year procedure", not this menu item.

Select printer

When you print reports from the program the report will always go to the Windows default printer using the default settings for paper size etc. If you want to direct the report to a different printer this must be selected from the available printers using this menu item before going to the report menu.

If you have faxing software loaded you will be able to send a fax from the program by selecting the fax "printer" before printing the report. Note that this also applies to other printed documents like statements for example.

Accounts menu items

Create, edit or delete an account

The program comes with a default set of basic account names, but you will want to delete some of these, add some new ones, or perhaps alter the names of some of the defaults. These functions are done through the "Accounts" menu. You cannot delete an account that contains transactions unless it has a zero balance, but you can change its name.

When you create an account you have to enter the account type as well as its name, for example:

Expenditure - Courier services
or
Income - Consultation fees

Transactions menu items

Before you begin entering any transactions you should read through the second part of this instruction book, entitled "Notes on Financial Statements". This explains the basics of how a set of books works for those who are not already experienced in this field.

When you click on the "Transactions" menu, you are given a few choices regarding how transactions may be entered. Each of these is designed for specific uses, but often more than one choice will do the job satisfactorily. The uses are:

1. Enter new transactions – general

    - This is usually used when none of the other more specific choices are suitable – such as for general "journal" transactions, reversing incorrect entries etc

    - More details on the use of the general transaction entry screen follow later.

2. Enter transactions from bank statement

    - This is one of the more common menu items you will select – you use it when you receive your bank statements and want to enter the transactions into EeziAccounts. It covers deposits and withdrawals, and you can easily select whether VAT is applicable or not. You also see a running total of the account displayed – this enables you to check whether your records agree with the bank's records.

3. Enter purchases subject to VAT

    - These transactions can usually be entered using the option above (from the bank statement), but if you wish to enter only

one or two such transactions, or maybe you haven't yet received the bank statement, then this option can be used

Enter new transactions – general

The program uses the double entry accounting system, meaning that for each debit there is a balancing credit. In laymen's terms, "money always comes from somewhere and goes somewhere".

For example, if a customer buys something and pays for it, you might debit "Cash on hand" and credit "Sales".

For a detailed description of the double entry accounting system, see the "Notes on Financial Statements" at the end of this booklet.

The screen has a Debit section coloured blue, and a Credit section coloured red. The following are the necessary steps to enter a transaction:

1. Choose the account type on the debit side (You can also start with the credit side if you want). For example, you might choose "Expenditure" as the account type.
2. Choose the account name, for example "Maintenance"
3. Type in a description of the transaction, like "Painting of offices".
4. Enter the debit amount.
5. Click on "Get date" and choose the correct date for this transaction.
6. Click the blue OK button. The info you entered will be written into the space provided on the debit side, and some of the details will also be

copied into the credit side of the screen. This is only to save you the effort of retyping, but if you want to perhaps have a different entry description for example, simply overwrite what was written there for you.

7. It is perfectly possible that you may have, say, three debits to balance one credit.

For example:

Debit:	Stationery	100
	Office flowers	200
	Meals	200
Credit:	Petty cash	500

8. You are not limited to posting only one transaction at a time. Each time you click the green or red OK buttons your entries are copied into the list. Once this is done new entry details can be filled in, and OK can be clicked again. This applies to both the debit and the credit sides.

9. In the middle of the screen at the top you are told whether your entries are balanced or not. If they are you may go ahead and post the entries to the accounts. Once you do this you cannot delete these entries, but you can of course enter correcting entries which reverse what you have done.

Using the wizard for transaction entry

On the "Enter transactions" screen is a "Help wizard" button which makes transaction entry much easier.
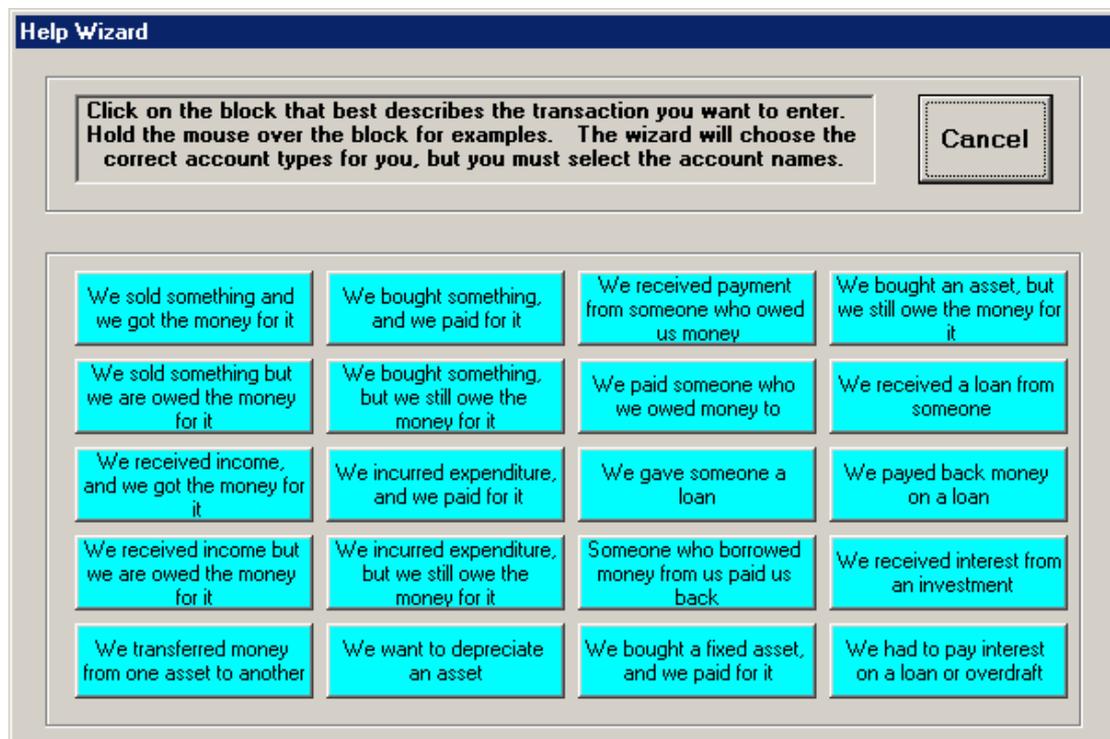
The screen offers you a lot of choices of typical simple transactions that you will probably have to process regularly. Some of these transactions would be easier to input using other parts of the program, but this is a good place to start learning the basics. The buttons explain the transaction, but you can also

get an example of the type of transaction by holding the mouse over the button for a couple of seconds.

Once you click on the button that describes your transaction, you will be given a little suggestions screen which tells you what you should do when you are taken back to the transaction entry screen. The wizard also chooses the account types for you, leaving you to choose the actual account names, and to fill in the remaining details.

Once transactions have been entered, the financial statements are automatically updated and are available for viewing on the main screen.

How do you start off your accounts the first time?

In most cases you will have an existing set of accounts that you are taking over from, or even if no formal accounts were kept, you will probably have a starting point where the company or club has an amount in the bank which is the total of its "accumulated funds" and its "share capital" (where applicable).

You start off your accounts by entering the following transaction, for example:

Debit: Current Asset - Cheque account   10 000
       Current Asset - Cash on hand   1 000

       Total   11 000

Credit: Capital - Accumulated funds brought forward   11 000

       Total   11 000

It is easiest to start from the last audited set of accounts that you have, but one could start from any point in time.

Enter purchases subject to VAT

This screen is used to easily enter purchases where part of the full purchase price is made up of Value Added Tax (VAT). Such transactions could be entered using the "Enter new transactions" screen, but then the VAT amount has to be manually calculated.

Included in this class of transactions are purchases which need to be allocated to an expenditure account, such as stationery, as well as purchases of Fixed or Current Assets like furniture or equipment.

NB - Purchases of stock should be entered using the Stock menu - the sub-menu being "Enter a stock movement". Stock purchased is one of the types of stock movement.

This screen requires that the total purchase price, transaction date and VAT rate must be entered. Defaults are provided.

Then the correct accounts must be selected - see the suggestions on account selection on the screen itself.

The user then enters the transaction description in the credit section. The credit section description is automatically copied to the VAT and debit

sections to save typing, but the VAT and debit descriptions can be edited or altered if necessary.

This screen processes one transaction at a time once the "Enter" button is clicked. Thereafter the necessary screen entries are cleared and the screen is ready to process the next transaction.

Enter transactions from bank statement

This screen is typically used at the end of the month once you receive your bank statements. In the top section you select the bank account that you are working on. The transactions for this account that have already been entered into the program will appear, and the balance of the account (according to the program) will be shown. You then go through your bank statement and enter any transactions that do not appear as having already been entered.

Transactions are entered as follows:

Enter the full amount, date and description in the boxes provided. Then select whether this is a deposit into the account, or a withdrawal from it. Then select whether VAT is applicable or not. If it is applicable another part of the screen appears in which you select the VAT account. Finally you select the account type and account name for the balancing account. For example if it is a withdrawal from the bank account to pay for stationery the balancing account will be "Expenditure – Stationery". Once all the data is correctly entered you click on Enter. The transaction will now appear in the upper section, and the

balance will be adjusted. This way you should be able to get the program's balance to agree with the balance on the statement once you have completed all entries. Of course this will not be the case if you have entered transactions into the program before they appear on the statement.

View all transaction entries

This brings up a screen showing all transaction entries for the current financial year, sorted by date. You are able to make changes to the transaction date and description, but not to any other fields. If you enter an incorrect transaction you have to do another transaction entry to reverse it. Whatever you debited originally you now credit, and whatever you credited you now debit.

Example

You make the following wrong entry (You put in R1000 instead of R100)

Debit: Expenditure   -   Postage   R1000
Credit: Current asset   -   Bank   R1000

Now you must enter the opposite transaction, namely:

Debit: Current asset   -   Bank   R1000
Credit: Expenditure   -   Postage   R1000

and finally you enter the correct transaction:

Debit: Expenditure   -   Postage   R100
Credit: Current asset   -   Bank   R100

This has the effect of removing the transaction entirely, although both the original transaction and the correction will appear in all reports etc. This is done because it should not be possible to remove or edit a transaction in a set of books without any evidence of the change remaining for auditors to be able to monitor.

Note that if you want a properly formatted report of all transactions for viewing or printing you should use the report menu.

Enter adjustments to last year's balances

This process is essentially exactly the same as entering new transactions in the current financial year, except that last year's final balances are affected, not the current year's figures. It is used in situations where perhaps the auditors suggest changes to last year's figures after you have already executed the end of year procedure and moved into the new year. It must be remembered that if any of these changes affect how the current balance sheet should read then the changes required to correct the current balance sheet must be made in this year's accounts as well.

Customers menu items

Enter new customer

This menu item brings up a new screen for entering customers. Simply fill in the required details as shown on the form.

Edit customer details

This brings up a screen which allows you to edit customer details previously entered.

Delete a customer

This menu item enables you to completely delete a customer. You simply have to select the required customer.

WARNING!! Note that all records for this customer will be deleted.

Invoices, credits and receipts

Generating an invoice

This screen is accessed from the customer menu.

The VAT rate is automatically entered, as is the date. You can enter a discount rate that will be applied to the entire invoice. You also need to select whether or not you want your banking details to appear on the invoice.

You now have to select the customer (or enter the account number) and enter the details of the Order Number, Quantity, Description and Price Each. If you have entered stock items manually, you only have to select the description - the price will be entered automatically.

Once all the fields are completed you click on the green Enter button. The details are now written into the grid below. If you notice an error after having entered items into the grid, double-click on the item concerned and you will be allowed to delete it. You then re-enter it correctly.

You can enter as many items as you wish on one invoice.

Once you have completed the entries you click on the "Process invoice" button. First you will be asked to confirm that the details are correct - **check carefully because after confirming you cannot edit the invoice.** You would have to issue a credit to remove it if you found an error later. Then you are asked how many copies should be printed - answer 0 if you don't want a printout.

You are then asked if you want to enter the amounts into the main company accounts. If you say no the balance sheet and income statement (as well as the ledger accounts etc) will remain unaffected. If you want the transaction to be reflected in the main accounts (which is normally the case), then reply "Yes".

If you reply "yes" you are taken to a new screen where you have to select the relevant accounts to post to. You are provided with suggestions which are typically the correct choices. The transaction descriptions are automatically entered for you, but you are able to edit them.

If your invoice was for an item that you keep in stock, you now need to go to the stock menu and generate a stock movement for stock sold. You are reminded of this as the screen closes.

Generating a credit note

The screens and procedures for generating credit notes are the same as those for invoices. See above.

Generating a receipt

In this case the receipt screen is a little simpler, but the process is very similar to that for invoices and credits.

Customer statements

View or print a single customer's statement

This menu item brings up a screen in which you select the customer you require, either by name or by account number. The screen also allows you to enter comments for the statement. These are of two types. The first is a comment that will only be displayed on the statement being called up, the second will display on all statements viewed or printed until such time as it is again changed or deleted.

If you view the statement it will be shown on screen, "To printer" obviously prints the statement directly. For an explanation of the facilities available at the bottom of the "View" screen, please see reports.

Print all customers' statements

Once again you are asked to enter/edit a comment that will appear on all statements. You are also asked whether or not you wish to print statements with zero balances.

Summary of statements

This allows you to view or print all customers' balances and age-analyses on one report.

Consolidate a single customer's statement (or all customers' statements)

This should only be used to remove old items from a customer's statement. Executing this function removes the details of all statement items before the date which you are asked to specify and combines those items into a single figure called "Balance brought forward". Typically it would be used to remove old items from a statement which is becoming too lengthy, especially if the items have been paid.

Note that this is not statement ageing. It is not necessary in this program to age statements, this is done automatically each time you view a statement.

Customer listing

This menu item produces a report (either viewed or printed) of all customer details such as address, phone number etc.

Stock menu items

Add, edit and delete suppliers

These three menu items allow you to enter the data relating to the suppliers of stock items. When you add stock items you will then be able to link the stock item to a supplier.

Add a new stock item

This menu item allows the entry of stock items. Whatever is added here can then be called up when entering an invoice.

You are asked for the following data:

- Description
- Stock category - You can divide stock into various categories of your choice. These are useful when reports are printed.
- Stock code - This is a specific code for each item
- Unit - This is the unit that the stock item is measured in. For example a liquid may be measured in millilitres (ml) or bottles or drums.
- Cost price - This must be entered per unit as described above
- Sale price - This is also per unit, and is exclusive of VAT
- Initial stock level - The amount of stock that you have when you start off the program.
- Supplier - This is either entered manually or selected from the suppliers already entered

Editing and deleting stock items

These are self-explanatory

End of year procedure

NOTE: This procedure must be done to close off a financial year before entering data for the new year. Adjustments to the previous year's final balances can be done at a later stage if necessary, but it is recommended to try and get the figures as close as possible to being correct before closing off.

This refers to the procedure that is carried out on the main company accounts at the end of the financial year. Clicking on this menu item does the following:

1. It reminds you to make a backup of the database. This must be done, preferably to stiffy disk as well as to a backup folder on the hard drive.
2. It prints out all your accounts and financial statements.
3. It transfers net income for the year to accumulated funds.
4. It removes all account entries for the year, and sets the balance of all income and expenditure accounts to zero.
5. All final balances from this year are stored and will be shown as the previous year's comparative figures once you move into the next year.

Reports menu items

Many different report options are provided. Each one offers the option of sending the reports direct to the printer, or to "Screen or file". When "to printer" is selected the report is directed to the printer without further intervention. Be sure to select the correct printer through the "Printer setup" menu item under the "File" menu.

When you select "to screen or file", the selected report is displayed on your screen. This enables you to view the report without printing it, but it also has a number of other features. Along the bottom of the screen is the following set of controls:

This is what each of these does:

This control allows you to browse through the various different pages of the report, or to cancel the compilation of a long report.

This control changes the display size of the report within the window

This control allows you to print the report. It offers the choice of pages to print, etc.

These controls offer the same features, they are just presented slightly differently. They enable you to export the report to many different common file formats, including Word®, Excel®, Lotus®, HTML (Internet web page format) and others. You are able to save the file to disk in any of these formats, or you are able to send the report out by email. To do this you have to have an email program set up as your default MAPI client. This can be done with Outlook Express® and most other major email programs. In Outlook Express®, click on Tools ... Options .... General, then click on "Make Outlook Express my default Simple MAPI Client"

Registration of the program

A registration card is provided that should be filled in and posted to the address provided. This will enable the supplier to give you telephonic support free of charge for sixty days and to notify you of updates and so on. When the free support period has expired, a support contract will have to be entered in to.

The following contacts should be used for support:

telephone: 074 568 5050
fax: 086 658 2874
email: support@eezisoft.co.za
regular post: Eezisoft CC, PO Box 752075, Gardenview ,2047, South Africa

Latest versions, updates etc

These will be made available from the web site at

http://eezisoft.co.za/

Notes on Financial Statements

The purpose of producing financial statements is to communicate financial information about a business. This communication process is achieved largely through two major reports, the balance sheet and the income statement (These are also called the financial statements).

The Balance Sheet (Statement of Financial Position)

If an individual wants to start his own business, a cash investment is typically required. With this money he may buy office equipment, inventory, machinery, land, and a building in which to operate his business. In buying these various items, the individual may run short of cash. As a result, he may go to a bank and arrange to borrow money. Upon receipt of the loan, he can then buy any additional business items needed. This simplified example illustrates what is included in an organisation's statement of financial position (a balance sheet). The three major financial items included in a balance sheet are assets, liabilities, and owners' equity. These financial items can be expressed by the following relationship, called the balance sheet equation:

Assets = liabilities + owners' equity

This is the logic behind this relationship:

Assets are economic resources of an organisation that are of value to the organisation. In the previous example, the cash invested, the office equipment, the machines, the land and the building are all examples of assets.

If we accept that all organisations need assets, it follows that these assets must come from somewhere. In other words, assets do not suddenly appear from thin air. One major source of an organisation's assets is the owner's (or owners') investment. In the original example at the beginning of this section, the individual started his own business by investing cash (an asset) into his business. Owners may also invest some of their personal non-cash assets (for example, a piece of land or equipment). The concept "owners' equity" represents the owners' interests in a business organisation. When the owners invest assets into an organisation their interest in the organisation increases. Conversely, when the organisation's assets are withdrawn by the owners, their interest in the organisation decreases. The other major activity which causes the owners' interests in a business organisation to change is when the income statement is analysed.

Thus, a major source of an organisation's assets is from the owners themselves. However, the owners may not have sufficient personal assets to completely operate their organisation. They may have to find an additional source of assets. The other major source of assets to an organisation is from "liabilities." In our example, the individual who started his own business organisation ran short of cash and obtained a bank loan. Upon granting the loan, the bank became another source of assets to the organisation. That is, the cash received from the bank increased the organisation's assets. The bank is an example of a liability source of assets. Liabilities typically represent

"debts owed to parties external to an organisation." (However, a company can have a liability to an internal party, for example, the salaries owed to its employees for work performed.) The bank from which the loan was obtained had no involvement with the business organisation prior to granting the loan and is thus considered an external source of assets. When owners invest assets into an organisation, they are considered an internal source of assets, since the owners are involved in the internal operating activities of the company.

Regardless of the size of a business organisation, the two major sources of assets are external sources (causing the incurrence of liabilities) and internal sources (the owners of the business organisation). We come back to the relationship (that is, the balance sheet equation) that we presented earlier:

Assets = liabilities + owners' equity

Another way of stating the above relationship would be Assets = equities.

In other words, for every business organisation asset, someone must have an interest (equity) in the asset. One of the interests is an external interest called liabilities, and the other is an internal interest called the owners. Conventionally, the word "equity" is not attached to the term "liabilities." However, we should think of the liabilities as being the other major equity source of an organisation's assets.

Below is a simplified example of a balance sheet for the Big Top Company on January 1, 1998, before the start of a new business organisation (but after the acquisition of various assets).

The Big Top Company
Balance Sheet
January 1, 1998

ASSETS		LIABILITIES & OWNERS' EQUITY	
Cash	R 100	Liabilities:	
Merchandise inventory	500	Loan from bank	R 600
Office supplies	200	Owners' equity:	
Machinery	600	Owners equity	1200
Land	400		
Total Assets	**R1800**	**Total liabilities and equity**	**R1800**

The Income Statement

A major reason why individuals start a business is to increase their assets. Initially, assets are invested into a new business organisation. Through subsequent operating activities, the owners hope to increase their assets. For example, the operating activity of a clothing store is to purchase clothing goods at wholesale prices and then to sell these goods at retail prices. The income statement gives relevant information regarding an organisation's success at increasing its assets or failure to increase them.

The two major financial items included in an income statement are revenues and expenses. Revenues, increases in a company's assets, are earned through selling a product or providing a service to someone. Earned revenues are positive occurrences to the owners of an organisation, since the

organisation's assets are increased as a result of the revenue earning function. The earning of revenues causes an "inflow of assets" into an organisation. If you walk into a department store and purchase some merchandise, the department store earns revenue at the time that it makes the sale to you. The revenue is earned by the department store when the sale is made whether you immediately pay cash or charge your purchase on a credit card. At the point of sale, you receive a service from the store of being able to buy and utilise its merchandise. Some individuals in the accounting profession favour the recognition of revenue prior to a sales transaction. However, only at the point of sale when an individual agrees to purchase an organisation's product at a specific price does objective evidence exist concerning the actual Rand amount of revenue earned.

Revenue recognition in a service industry is illustrated by the television repairman who earns revenue through fixing customers' TV sets. Upon repairing someone's television set and billing the customer (for example, a R25 service bill), the repairman earns the R25 even if the cash is not immediately received. It is the act of providing the service that earns the revenue for the repairman.

As discussed previously, earned revenues represent increases in an organisation's assets and are thus positive events to the owners. Earned revenues can be thought of as the accomplishments of an organisation. However, in order to have these accomplishments, certain efforts must be put forth. The efforts that a business organisation puts forth in attempting to earn revenues are called expenses. Expenses represent a decrease in an organisation's assets (either currently or at a future time). They are caused by receiving benefits from someone or something as an aid in earning revenues. Ideally, a business organisation would like to incur no expenses, since they eventually result in an outflow (decrease) of assets. Thus, expenses are a negative activity from the owners' point of view. It is impossible, however, to operate a business organisation without incurring expenses. An organisation receives different types of benefits, which cause different types of expenses. For example, the benefits received from leasing building space to operate your business results in "rent expense." The benefits received from having employees work for you results in "salaries expense." Organisations incur expenses upon receiving benefits from someone or something, regardless of whether cash is immediately paid for the benefits received. If an individual provides a company benefits by working as an employee but has not yet been paid, then the company has a liability to eventually pay the employee cash. In this case, the asset cash is not immediately decreased as a result of the expense. However, as soon as the company pays the employee, its assets decrease. If we think of revenues as accomplishments and expenses as efforts, the objective of an organisation is to have the accomplishments exceed its efforts (that is, the revenues exceed its expenses). When this happens, the organisation earns a net income.

An organisation's net income causes an overall increase in its assets from business operations, as shown below:

Revenues (accomplishments): increase in assets from business operations

Less: Expenses (efforts): decrease in assets from business operations

Equals: Net income (accomplishments exceed efforts): overall increase in assets from business operations

Net income does not represent an increase in just the asset cash. Rather, any or all of a company's assets may increase from earning a net income. The important point to remember is that net income represents an overall increase in a company's assets and this increase can be reflected in various assets. For example, a portion of an organisation's net income may be used to purchase additional equipment (which is an asset). Conversely, if more efforts (expenses) are put forth than accomplishments (revenues), a company has a net loss. The effect of an organisation's net loss is to cause a decrease in its assets. An organisation attempts to perform its operating activities in a manner to avoid a net loss.

An organisation's net income is the reward to the owners from successful operation of their business organisation. Thus, the increase in assets caused by earning a net income goes to the owners and increases their equity in the organisation. The balance sheet classification called owners' equity is increased as a result of a company's earning a net income. On the other hand, if a company incurs a net loss (a decrease in assets), the owners must absorb the loss. Therefore, the effect of a net loss from business operations is the reduction of the owners' equity.

Continuing the example of the Big Top Company, the diagram reflects the company's income statement for January 1998, the first month of business.

The Big Top Company

Income Statement for the Month Ended January 31, 1998

Revenues

Retail price of merchandise sold	R5000

Less: Expenses

Cost of merchandise sold	R2920
Salaries to employees	1400
Rent on the store and office facilities	500
Advertising in the newspaper	75
Interest on cash borrowed from the bank	5

Total expenses	R4900
Net income	R 100

The heading of the income statement indicates the name of the company, the title of the statement, and the period of time for which the analysis is prepared. The first major category on the income statement is the revenue

earned, which represents the increase in the company's assets from the sale of its merchandise at retail prices.

The second major category indicates the efforts (expenses) put forth to earn the revenues. As previously discussed, expenses represent decreases in a company's assets as a result of receiving benefits from someone or something. The R2920 "cost of merchandise sold" is the wholesale cost to the Big Top Company of the merchandise that was sold. The retail price of this merchandise was R5000, the revenue item reported on the income statement. The "salaries expense" of R1400 represents the benefits received by the Big Top Company from the employees that worked for the organisation during January. The R500 rent is an expense, since the Big Top Company received benefits during January from using the rented store and office facilities to operate its business organisation. The Big Top Company has R75 "advertising expense" from announcements in the local newspaper publicising the company's products. The R5 "interest expense" is caused by the company's bank loan. Interest on a bank loan is an expense resulting from the privilege of being able to borrow money for a designated time period.

Since the Big Top Company's revenues are R100 greater than its expenses during January, the resultant R100 net income causes the owners' interests (represented by the "owners' equity" on the balance sheet) in the company's assets to increase by R100. Thus, the income statement gives interested parties relevant information concerning the success of an organisation in increasing its assets from operating activities.

Relationship of Income Statement to Balance Sheet

The next figures show the Big Top Company's statement of financial position (balance sheet) on January 31, 1998, after the January net income of R100 was determined from the company's income statement.

The Big Top Company Balance Sheet January 31, 1998

ASSETS

Cash	R 200	
Accounts receivable	150	
Merchandise inventory	200	
Office supplies	300	
Machinery	650	
Land	400	
Total Assets		R1900

LIABILITIES & OWNERS' EQUITY

Liabilities:

Accounts payable	R 400	
Loan from bank	200	
Total liabilities		R600

Owners' equity:

Investment by the owners	R1200
Plus: Net income for the month of January	R100
Owners' equity, January31, 1998	R1300
Total liabilities and owners' equity	R1900

The Big Top Company's total assets increased from R1800 on January 1 to R1900 on January 31. This R100 increase was caused by the R100 earned net income. The R100 increase in total assets is also reflected as a R100 increase in the "owners' equity," since the owners receive the net income. As a result of both the assets and the owners' equity increasing by R100, the balance sheet equation (Assets = liabilities + owners' equity) and the balance sheet (which is based upon the equation) will continue to "balance." Before the net income is formally computed at month's end on the income statement, it is already included among the company's various assets. For example, a portion of the net income may have been used during the month to buy additional machinery, causing an increase in the asset "machinery." However, the total net income is not reflected as an increase in the owners' equity until it is computed on the income statement and then transferred to the balance sheet. After this is accomplished, both the assets and the owners' equity will

have the net income included in their total monetary figures, and the statement of financial position (balance sheet) will 'balance." Thus, the connecting link between the income statement and the balance sheet is through the net income figure. The income statement must be prepared first. Then, the computed net income is added to the owners' equity section of the balance sheet in order to complete the financial statements.

Two new items illustrated on the Big Top Company's January 31, 1998 balance sheet are the asset "accounts receivable" and the liability "accounts payable." An account receivable means that somebody owes the Big Top Company cash. Receivables result from the sale of the company's products without immediately collecting the cash. For example, if you go into a department store, buy a R25 radio, and use your credit card to make the purchase rather than paying cash, the department store has a R25 account receivable against you. Since some individuals to whom sales have been made have not yet paid for the products purchased, the Big Top Company has a R150 asset claim against these customers for the cash that will eventually be paid to the company.

The R400 accounts payable on the balance sheet means that the Big Top Company bought something and did not immediately pay cash for the items purchased. The Big Top Company thus has a liability to eventually pay for the purchased goods. As soon as the company makes payment, its liability will be eliminated. As can be seen, an account receivable and an account payable are opposites. An account receivable means that somebody owes the Big Top Company cash and is thus an asset, whereas an account payable means that the Big Top Company owes somebody cash and is thus a liability. In the previous paragraph's example of your buying a R25 radio from a department store and charging the purchase, the store has a R25 account receivable against you. However, from your point of view as the buyer of the radio, you have a R25 account payable (a liability) to pay the store R25 cash.

A comparison of the Big Top Company's balance sheets on January 1 and January 31 reveals that the bank liability for the R600 loan was reduced to R200 by January 31. In other words, the Big Top Company decreased its bank debt during January by paying the bank R400. The only asset that did not change from January 1 to January 31 was the "land," which remained at R400 during the entire month.

In summary, a large amount of valuable information can be obtained from the income statement and the balance sheet. The former provides useful information about a company's operating activities; the latter discloses relevant information concerning the company's financial position.

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