**ECONOMIC AND MANAGEMENT SCIENCES**

**GRADE 9**

**TERM 2**

Financial Literacy – ACCOUNTING EQUATION (credit sales):

**Learners should achieve the following outcomes, as per CAPS:**

* Effect of cash transactions (credit sales) on the accounting equation
* Assets = Owner’s equity + Liabilities (A = OE + L)

**INTRODUCTION:**

In accounting there are different accounts involved with a transaction. All transactions should be recorded and there are always TWO accounts involved with the recording of that transaction.

One account should be debited whilst the other account is credited. This is known as the double entry principle.

**What is the Accounting equation?**

All accounts in accounting are classified as assets, owner’s equity or liabilities.

When transactions are recorded, there will be a change in assets, owner’s equity or liabilities – depending on which type of accounts are involved.

The accounting equation is as follows:

**Assets = Owner’s equity + Liabilities (A=OE+L)**

In an equiation the side before the equation sign (=) should be the same as the side after the equation sign.

In other words, the effect on assets should be the same as the effect on owner’s equity and liabilities.

It is very important to know the two accounts involved in a transaction as well as how these accounts will be classified.

**Examples: Classification of accounts:**

|  |  |  |  |
| --- | --- | --- | --- |
| **ASSETS** | | **LIABILITIES** | |
| **Current assets** | **Non-current assets** | **Current liabilities** | **Non-current liabilities** |
| Cash/ Bank | Land and Buildings | Short term loans | Long term loans |
| Debtors | Vehicles | Bank overdraft |  |
| Trading stock | Equipment |  |  |
|  |  |  |  |
| **OWNER’S EQUITY** | | **INCOME** | **EXPENSES** |
| Capital | | Rental income | Rent expense |
| Drawings | | Current income | Trading licence |
|  | | Commission income | Water en electricity |
| Interest received | Wages |
| Sales | Stationery |
|  | Advertising |
|  | Interest paid  Cost of sales |

**What is credit sales?**

Credit sales occur when a business allows customers to buy goods on credit and to pay for these goods at a later stage.

When goods are sold on credit, two things happen:

1. The business’ sales increase.
2. The business’ stock decrease.

**Credit sales transaction: Four accounts involved:**

1. Account Debited: Debtors Control (Debtors increase) (A+) Account Credited: Sales (Income increases Owner’s Equity) (OE+)
2. Account Debited: Cost of sales (Expenses decrease Owner’s Equity) (OE–) Account Credited: Trading stock (Stock decreases) (A–)

**Effect of credit transactions on the accounting equation:**

1. **Effect of credit sales:**

**Transaction:** Sell goods valued at R3 000 on credit to B. Saul. The cost price of these goods amount to R1 700.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Account DR** | **Account CR** | **ASSETS** | | **OWNER’S EQUITY** | | **LIABILITIES** | |
| **Effect** | **Reason** | **Effect** | **Reason** | **Effect** | **Reason** |
| Debtors Control | Sales | +R3000 | Debtors increase | +R3000 | Income increase | 0 |  |
| Cost of sales | Trading stock | -R1700 | Stock decreases | -R1700 | Expenses increase | 0 |  |

**Explanation:**

* When the business sells goods on credit, the debtor’s account increase, hence debtors control (asset) will be debited and income from sales (income) will be credited.
* Every time when goods are sold, stock on the shelves will decrease, that is why trading stock (asset) will be credited and the cost of the sold items (cost of sales) will increase, hence cost of sales (expense) will be debited.

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Financial literacy – ACCOUNTING EQUATION (credit sales):

**Activity 1: Concepts relating to the accounting equation**

Match the descriptions in Column B with the correct term/s in Column A. Write only your correct answer in the Answer Column. E.g. 1.1. E.

|  |  |  |  |
| --- | --- | --- | --- |
| **NO** | **COLUMN A** | **COLUMN B** | **ANSWER** |
| 1.1. | A = OE + L | 1. Refers to the capital contribution made by an owner and it is increased by profits. |  |
| 1.2. | Assets | 1. The accounting equation should always balance. |  |
| 1.3. | Owner’s equity | 1. Examples hereof are equipment and vehicles. |  |
| 1.4. | Liabilities | 1. All the ….. received by a business will increase owner’s equity. |  |
| 1.5. | Income | 1. A loan that is granted to a business will increase ….. |  |

**Activity 2:**

**Effect of credit sales transactions on the accounting equation**

Show the effect of the following credit sales transaction on the accounting equation.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| No | Transaction | Effect on the accounting equation | | |
| ASSETS | OWNER’S EQUITY | LIABILITIES |
| 2.1 | Sell goods on credit to Aby. Selling price: R5 200 Cost price: R3 150 |  |  |  |
|  |  |  |
| 2.2 | Goods with a selling price of R8 250 are sold on credit to Sammy. The cost price of these goods were R4 100. |  |  |  |
|  |  |  |
| 2.3 | Sell goods with a selling price of R6 000 on credit to Joan. Profit mark-up: 25% |  |  |  |
|  |  |  |

**Activity 3:**

**Effect of credit sales transactions on the accounting equation**

Show the effect of the following credit sales transactions on the accounting equation.

3.1. Sell goods on credit to Mr Botha, R3 250. Cost price: R1 600.

3.2. Issue an invoice valued at R4 500 to John. 20% profit was added to the cost price.

3.3. The trading stock reduced with R2 000 after Lucy bought goods on credit at Top Books. Top Books uses a 50% profit mark-up.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **No** | **ASSETS** | | **OWNER’S EQUITY** | | **LIABILITIES** | |
| **Effect** | **Reason** | **Effect** | **Reason** | **Effect** | **Reason** |
| 3.1 |  |  |  |  |  |  |
|  |  |  |  |  |  |
| 3.2 |  |  |  |  |  |  |
|  |  |  |  |  |  |
| 3.3 |  |  |  |  |  |  |
|  |  |  |  |  |  |

**Activity 4:**

**Effect of credit sales transactions on the accounting equation**

Study the accounting equation below and answer the following questions.

|  |  |  |  |
| --- | --- | --- | --- |
| Transaction | Effect on the accounting equation | | |
| ASSETS | OWNER’S EQUITY | LIABILITIES |
| Sell goods on credit to Aby. Selling price: R4 000  Cost price: R1 500 | +R4 000 | +R4 000 | 0 |
| -R1 500 | -R1 500 | 0 |

* 1. Why did assets increase with R4 000?

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* 1. What was the effect on the total of trading stock after the sales transaction?

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* 1. Why did owner’s equity decrease with R1 500?

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* 1. Calculate the profit that was made by the business with this sales transaction.

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