

Lecture 9: Revenue Cycle Applications

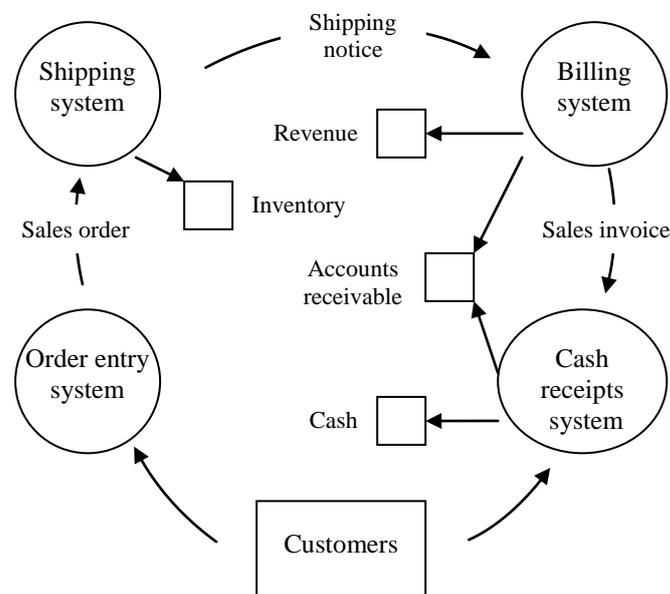
Learning Objectives

1. To review the accounting entries recorded in the revenue cycle.
2. To learn which documents, reports and records are used in the revenue cycle.
3. To understand how accounting transactions are processed by the application systems in the revenue cycle.
4. To see how control practices and procedures are applied in the revenue cycle.

The revenue cycle processes accounting transactions that record four economic events:

- a) **The request for goods or services by a customer.** Computer-based systems use an *order entry application system* to record these request
- b) **The delivery of goods or services.** When goods are involved, a *shipping application system* records this event.
- c) **The request of payment.** This economic event is processed by the *billing system*.
- d) **The receipt for payment.** To record this event is used a *cash receipts application system*.

Illustration 9.1: Application systems in the Revenue Cycle



Source: BOOCKHOLDT, J.L. *Accounting Information Systems: transaction processing and controls*. 5th edition, Boston: McGraw Hill Education 1999, ISBN 0-07-116098-1

In the revenue cycle occurs routinely a series of transactions. This article describes these transactions and show the documents used by the accounting system in recording them.

Credit Sales

Most businesses sell to their customers on credit. The general ledger entry recording such a sale is:

Debit	Credit
Accounts Receivable \$xxx	Sales \$xxx

An accounting system records a credit sale in general and subsidiary ledgers using three documents:

- **Sales order** – a document on which a sales department records an order from a customer
- **Shipping notice** – a document completed by the shipping department to notify the billing department that a shipment has been made
- **Sales invoice** – a document mailed to customers informing them of the amount due

Cash Receipts

Businesses receive cash in return for their goods or services from two sources:

1. Cash Receipts from Credit Sales – the accounting entry recording a customer’s payment for a sale made on credit is:

Debit	Credit
Cash \$xxx	Accounts Receivable \$xxx

Businesses ask customers to return a document called a **remittance advice** with their payments. This document is the system’s source of data for making the entry in the accounts receivable subsidiary record.

2. Cash Receipts from Cash Sales – the required accounting entry to record a cash sale is:

Debit	Credit
Cash \$xxx	Sales \$xxx

A sales clerk enters the amount of the sale on a **sales ticket**.

Sales Returns

Sales return occurs when a customer returns merchandise to the seller. The entry recording a sales return is:

Debit	Credit
Sales Returns \$xxx	Accounts Receivable \$xxx

The accounting system documents a sales return with a **credit memo**.

Sales Allowances

A sales allowance occurs when the sale department agrees to give the customer credit for items that were not returned. The entry for a sales allowance is:

Debit		Credit	
Sales Allowances	\$xxx	Accounts Receivable	\$xxx

The sales department prepares a memo explaining why the credit to the customer's account is justified. This initiates the preparation of a *credit memo*.

Bad Debt Write-Offs

When a business determines that the cash from a credit sale will never be received, management may choose to give up effort at collecting it and assume that it is a bad debt. The entry to record a bad debt write-off is:

Debit		Credit	
Allowance for Doubtful Accounts	\$xxx	Accounts Receivable	\$xxx

The credit manager documents the inability of the customer to collect the account in a *memo*. The treasurer authorizes the write-off by approving the memo and the accounting department prepares a *journal voucher* to record it in a general ledger.

Revenue Cycle Reports

Application systems in the revenue cycle produce three kinds of reports:

1. **Control Reports** – is used whenever the accounting systems process multiple changes to a file.
2. **Registers** – is a listing of all the transaction of a certain type that were processed during a single processing period.
3. **Special Purposes Reports** – most systems require three special purpose accounting reports:
 - **Customer Statement** – a list of all transactions in a customer's account during a specified time period.
 - **Aged Accounts Receivable Trial Balance** – a list of all customers and the balances (categorized according to how long it has existed) they owe at a specified date.
 - **Remittance List** – a list of all currency and checks received during one day.

Revenue Cycle Accounting Records

Accounting systems maintain records in manual journals and ledgers (*noncomputerized records*) or in computer files and databases (computerized records). The most applied way of accounting records is a *computer-based accounting system* that uses both computerized and manual processes.

In the revenue cycle, a computer-based system uses four application systems:

- **Order Entry Application** – the purpose of this application is to record a customer's request for goods or services, to obtain credit approval for the customer and ensure that the order is filled.
- **Shipping Application** – this application is used to ensure that merchandise is shipped prior to the date desired by the customer and that the customer is promptly billed for the merchandise.
- **Billing Application** – the purposes of this application are to prepare sales invoices for merchandise that has been shipped and to record the sale in the appropriate accounts. It produces also credit memos to document sales returns and sales allowances.
- **Cash Receipts Application** – the application is used to record payment made by customers for credit sales.

Lecture 9 - Questions and exercises

Q 9-1: Which economic events produce transaction in the revenue cycle?

Q 9-2: What is the purpose of each of the following documents?

- a) Sales order
- b) Shipping notice
- c) Sales invoice
- d) Credit memo

Q 9-3: Which six types of transaction do accounting systems record in the revenue cycle?

Q 9-4: Which three special purposes reports produce application systems in the revenue cycle?

E 9-1: Transactions and documents

The column on the left lists accounting transactions processed in the revenue cycle. In the right column is a list of documents a de reports. Identify the document(s) and report(s) associated with each transaction.

- | | |
|-------------------------|------------------------|
| a) Credit sale. | 1. Aged trial balance. |
| b) Bed debts write-off. | 2. Credit memo. |
| c) Sales return. | 3. Sales ticket. |
| d) Cash sale. | 4. Remittance advice. |
| e) Sales allowance. | 5. Sales order. |
| f) Payment on account. | 6. Sales invoice. |

The main source:

BOCKHOLDT, J. L. *Accounting Information Systems: transaction processing and controls*. 5th edition, Boston: McGraw Hill Education 1999, ISBN 0-07-116098-1

The supplementary sources:

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