

Recording Business Transactions

Chapter 2

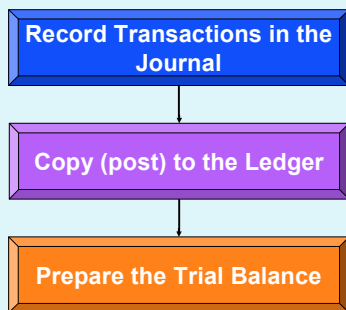
Learning Objective 1

Explain accounts, journals, and ledgers as they relate to recording transactions and describe common accounts

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The Accounting Process



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Account

- ▶ Basic summary device
- ▶ Detailed record of increases and decreases in specific assets, liabilities, or owner's equity during a period

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Journal and Ledger

- ▶ Journal
 - Chronological record of transactions
 - Organized by date
- ▶ Ledger
 - Book (or computer record) of all account activity
 - Organized by account

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Trial Balance

- ▶ Listing of all accounts and their balances

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Accounting Equation

Accounts are grouped in 3 broad categories:

$$\text{Assets} = \text{Liabilities} + \text{Owner's equity}$$

Assets

Economic resources that will benefit the business in the future

Liabilities

Creditors' claims to assets (debt)

Owner's Equity

Owner's claim to the assets

- ▶ Capital
- ▶ Withdrawals
- ▶ Revenues
- ▶ Expenses

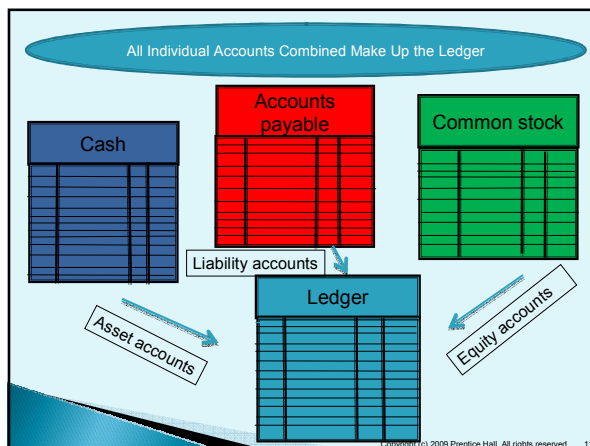


Chart of Accounts

- ▶ List of all accounts used by a company along with the account numbers

Acct. #	Account title
101	Cash
111	Accounts receivable
150	Equipment
201	Accounts payable
301	Common stock
305	Retained earnings
401	Service revenue
501	Rent expense
525	Advertising expense

Learning Objective 2

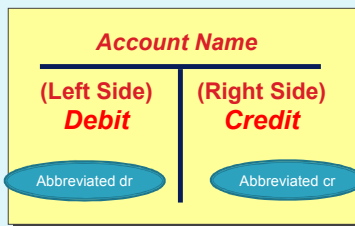
Define debits, credits, and normal account balances. Use double entry accounting and T-accounts.

Double Entry System

- ▶ Record dual effects of each transaction
- ▶ Each transaction has a:
 - Receiving side
 - Giving side

T-Account

Simple tool for analyzing and determining the balance in a given account



Increase and Decreases in Accounts

- ▶ Whether an account is increased by debit or a credit is determined by the account type
 - Asset, liability, or equity
- ▶ Debits are not good or bad

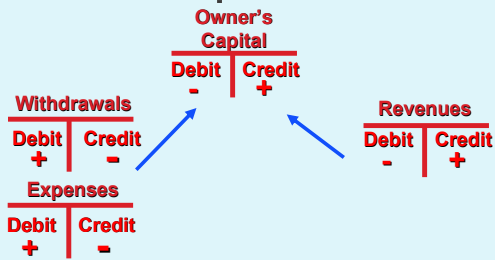
Rules of Debit and Credit

Assets		=	Liabilities		+	Owner's equity	
Debit	Credit		Debit	Credit		Debit	Credit
+	-		-	+		-	+

Normal Balances

Assets		=	Liabilities		+	Equity	
Debit	Credit		Debit	Credit		Debit	Credit
+	-		-	+		-	+
↑			↑			↑	
Normal Balance			Normal Balance			Normal Balance	

Expanding Debit/Credit Rules Revenues & Expenses

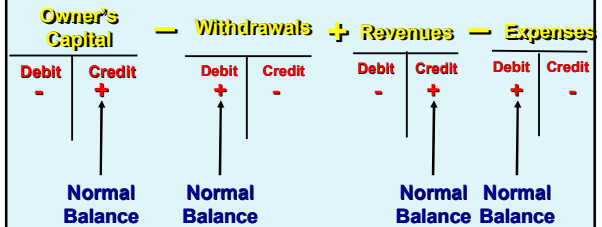


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Normal Balances

Owner's equity



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20

Debit

- ▶ Assets
- ▶ Withdrawals
- ▶ Expenses

Credit

- ▶ Liabilities
- ▶ Capital
- ▶ Revenues

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21

T-Account Example

Cash	
\$20,000	\$12,000
\$8,000	

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Learning Objective 3

List the steps of the transactions to the ledger

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Journalizing Process

Identify each account affected and its type

Determine if each account is increased or decreased

Record transaction in the journal

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Journal Entry

- ▶ Four parts:
 - Date of transaction
 - Title of account debited with dollar amount
 - Title of account credited with dollar amount
 - Brief explanation of transaction

General Journal

Transaction Date		Accounts Affected	
Journal Page 1			
Date	Description	Debit	Credit
Jul 1	Cash	45,000	
	Josie Smith, Capital		45,000
	Owner investment		

Explanation of transaction

Dollar amount of debits and credits

Posting

- ▶ Copying amounts from the journal to the ledger

Short Exercise 2-6

- March 22:
- ▶ "On account" indicates Accounts receivable
 - ▶ Accounts receivable is an asset account
 - ▶ Increase an asset with a debit

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
Mar 22	Accounts receivable		4,000	

Short Exercise 2-6 (continued)

- March 22:
- ▶ "Performed services" indicates revenue has been earned
 - ▶ Revenues are increased by credits

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
Mar 22	Accounts receivable		4,000	
	Service revenue			4,000
	Performed services on account			

Short Exercise 2-6 (continued)

- March 30:
- ▶ Cash is received
 - ▶ The payment is "on account"

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
Mar 30	Cash		3,000	
	Accounts receivable			3,000
	Received payment on account			

Short Exercise 2-6 (continued)

March 31:

- ▶ A utility bill is an expense
- ▶ The bill will be paid later – creating an account payable

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
Mar 31	Utilities expense		130	
	Accounts payable			130
	<i>Received utility bill</i>			

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31

Short Exercise 2-6 (continued)

March 31:

- ▶ Salaries to employees are an expense
- ▶ The salary was paid in cash

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
Mar 31	Salaries expense		2,300	
	Cash			2,300
	<i>Paid salaries</i>			

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32

Short Exercise 2-6 (continued)

March 31:

- ▶ Advertising is another expense
- ▶ Cash is paid

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
Mar 31	Advertising expense		400	
	Cash			400
	<i>Paid advertising</i>			

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33

Source Documents

- ▶ Origin of accounting transactions

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Learning Objective 4

Journalize and post sample transactions to the ledger

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Short Exercise 2-8

Cash	Accounts receivable	Service revenue

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
	Accounts receivable		9,000	
	Service revenue			9,000
	<i>Performed legal services on account</i>			

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36

Short Exercise 2-8 (continued)

Cash	Accounts receivable	Service revenue
	9,000	9,000

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
	Accounts receivable		9,000	
	Service revenue			9,000
	<i>Performed legal services on account</i>			

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37

Short Exercise 2-8 (continued)

Cash	Accounts receivable	Service revenue
	9,000	9,000

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
	Cash		5,400	
	Accounts receivable			5,400
	<i>Received payment on account</i>			

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38

Short Exercise 2-8 (continued)

Cash	Accounts receivable	Service revenue
5,400	9,000	9,000
	5,400	
	3,600	

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
	Cash		5,400	
	Accounts receivable			5,400
	<i>Received payment on account</i>			

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Learning Objective 5

Prepare the trial balance from the T-Accounts

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Trial Balance

- ▶ Summary of the ledger
- ▶ Lists all accounts with their balances
- ▶ Accuracy check
 - Debits should equal credits
- ▶ NOT a balance sheet

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41

Locating Trial Balance Errors

- ▶ Search for missing account
- ▶ Divide the difference between debits and credits by two
- ▶ Divide out of balance amount by nine

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42

Details of the Journal

Date of transaction

Posting reference

GENERAL JOURNAL				
DATE	DESCRIPTION	REF	DEBIT	CREDIT
Jan 2	Cash		1,000	
	Josie Smith, Capital			1,000

Accounts debited and credited

Amounts debited and credited

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Details of the Ledger

GENERAL JOURNAL Page 1

DATE	DESCRIPTION	POST REF	DEBIT	CREDIT
Jan 2	Cash	101	1,000	
	Josie Smith, Capital	301		1,000

1 2 3 4 5

Cash Account No. 101

Date	Jrnl. Ref.	Debit	Date	Jrnl. Ref.	Credit
2-Jan	J.1.	1,000			

Josie Smith, Capital Account No. 301

Date	Jrnl. Ref.	Debit	Date	Jrnl. Ref.	Credit
			2-Jan	J.1.	1,000

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Four-Column Account

CASH Acct No. 101

Balance

Date	Item	Jrnl Ref	Debit	Credit	Debit	Credit
1-Apr		J.1	20,000		20,000	
3-Apr		J.1		9,000		11,000
5-Apr		J.1	3,000		14,000	
6-Apr		J.1	10,000		4,000	

Alternative to the T-Account

End of Chapter 2