

# College Accounting

A Contemporary Approach

Fourth Edition

Haddock | Price | Farina

Mc  
Graw  
Hill  
Education

# **Chapter 3**

## **Analyzing Business Transactions Using T Accounts**

**by**  
**Haddock, Price, and Farina**

# Chapter 3 Learning Objectives

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## **SECTION 1: Transactions That Affect Assets, Liabilities, and Owner's Equity**

- 3-1 Set up T accounts for assets, liabilities, and owner's equity.**
- 3-2 Analyze business transactions and enter them in the accounts.**
- 3-3 Determine the balance of an account.**

## **SECTION 2: Transactions That Affect Revenue, Expenses, and Withdrawals**

- 3-4 Set up T accounts for revenue and expenses.**
- 3-5 Prepare a trial balance from T accounts.**
- 3-6 Prepare an income statement, a statement of owner's equity, and a balance sheet.**
- 3-7 Develop a chart of accounts.**
- 3-8 Define the accounting terms new to this chapter.**

# Section 1: Transactions That Affect Assets, Liabilities, and Owner's Equity

## Learning Objective

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**3-1: Set up T accounts for  
assets, liabilities, and owner's  
equity.**

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# The Accounting Equation

## ASSETS

The property a  
business owns

=

## LIABILITIES

The debts of  
the business

+

## OWNER'S EQUITY

The owner's financial  
interest in the business

# Classification of Accounts

- **Asset Accounts**  
Asset accounts show the property a business owns.
- **Liability Accounts**  
Liability accounts show the debts of the business.
- **Owner's Equity Accounts**  
Owner's equity accounts show the owner's financial interest in the business.

# T Accounts

Accountants use *T accounts* to analyze transactions. A *T account* consists of a vertical line and a horizontal line that resembles the letter T. *T accounts* are helpful when analyzing transactions.

These are examples of *T accounts* for assets, liabilities, and owner's equity.

<b>ASSETS</b>	<b>=</b>	<b>LIABILITIES</b>	<b>+</b>	<b>OWNER'S EQUITY</b>
<div style="display: flex; justify-content: space-between;"> <div style="text-align: center; width: 45%;"> <p><b>+</b> Record Increases</p> <p><b>LEFT SIDE</b></p> </div> <div style="text-align: center; width: 45%;"> <p><b>-</b> Record Decreases</p> <p><b>RIGHT SIDE</b></p> </div> </div>		<div style="display: flex; justify-content: space-between;"> <div style="text-align: center; width: 45%;"> <p><b>-</b> Record Decreases</p> <p><b>LEFT SIDE</b></p> </div> <div style="text-align: center; width: 45%;"> <p><b>+</b> Record Increases</p> <p><b>RIGHT SIDE</b></p> </div> </div>		<div style="display: flex; justify-content: space-between;"> <div style="text-align: center; width: 45%;"> <p><b>-</b> Record Decreases</p> <p><b>LEFT SIDE</b></p> </div> <div style="text-align: center; width: 45%;"> <p><b>+</b> Record Increases</p> <p><b>RIGHT SIDE</b></p> </div> </div>

# Section 1: Transactions That Affect Assets, Liabilities, and Owner's Equity

## Learning Objective

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**3-2: Analyze business transactions and enter them in the accounts.**

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# Effects of Business Transactions

**Steps to analyze the effects of the business transactions:**

- 1. Analyze the financial event.**
  - Identify the accounts affected.
  - Classify the accounts affected.
  - Determine the amount of increase or decrease for each account.
- 2. Apply the *left-side-right-side* rules for each account affected.**
- 3. Make the entry in T-account form.**

# Initial Investment

Trayton Eli withdrew \$100,000 from personal savings and deposited it in the new business checking account for Eli's Consulting Services.

- **LEFT** Increases to asset accounts are recorded on the left side of the T account.
- **RIGHT** Increases to owner's equity accounts are recorded on the right side of the T account.

<b>Cash</b>	<b>Trayton Eli, Capital</b>
(a) 100,000	(a) 100,000

# Business Transaction

**Eli's Consulting Services issued a \$5,000 check to purchase a computer and other equipment.**

**Analysis:**

**(b) The asset account, Equipment, is increased by \$5,000.**

**(b) The asset account, Cash, is decreased by \$5,000.**

**Equipment**

**(b) 5,000**

**Cash**

**(b) 5,000**

# Purchase of Equipment on Account

The firm bought office equipment for \$6,000 on account from Office Plus.

Analysis:

(c) The asset account, Equipment, is increased by \$6,000.

(c) The liability account, Accounts Payable, is increased by \$6,000.

<b>Equipment</b>	
(c) 6,000	

<b>Accounts Payable</b>	
	(c) 6,000

# Purchase of Supplies for Cash

**Eli's Consulting Services issued a check for \$1,500 to Office Delux Inc. to purchase office supplies.**

**Analysis:**

**(d) The asset account, Supplies, is increased by \$1,500.**

**(d) The asset account, Cash, is decreased by \$1,500.**

<b>Supplies</b>	
<b>(d) 1,500</b>	

<b>Cash</b>	
	<b>(d) 1,500</b>

# Payment of a Liability

**Eli's Consulting Services issued a check in the amount of \$2,500 to Office Plus.**

**Analysis:**

**(e) The asset account, Cash, is decreased by \$2,500.**

**(e) The liability account, Accounts Payable, is decreased by \$2,500.**

<b>Accounts Payable</b>	
<b>(e) 2,500</b>	

<b>Cash</b>	
	<b>(e) 2,500</b>

# Prepayment of Rent

**Eli's Consulting Services issued a check for \$8,000 to pay rent for the months of December and January.**

**Analysis:**

**(f) The asset account, Prepaid Rent, is increased by \$8,000.**

**(f) The asset account, Cash, is decreased by \$8,000.**

<b>Prepaid Rent</b>	
<b>(f) 8,000</b>	

<b>Cash</b>	
	<b>(f) 8,000</b>

**Section 1: Transactions That Affect Assets,  
Liabilities, and Owner's Equity**

**Learning Objective**

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**3-3: Determine the balance of an  
account**

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**An account balance is the difference between the amounts recorded on the two sides of an account.**


**A footing is a small pencil figure written at the base of an amount column showing the sum of the entries in the column.**

# Recording Account Balances

<b>IF</b>	<b>THEN</b>
the total on the right side is larger than the total on the left side,	the balance is recorded on the right side.
the total on the left side is larger,	the balance is recorded on the left side.
an account shows only one amount,	that amount is the balance.
an account contains entries on only one side,	the total of those entries is the account balance.

# Computing the Account Balance

## Cash

(a) 100,000	(b) 5,000
	(d) 1,500
	(e) 2,500
	(f) 8,000
	-----
	17,000
<b>Bal. <u>83,000</u></b>	 <b>Footing</b>
(100,000 – 17,000)	

# Summary of Account Balances

ASSETS	=	LIABILITIES	+	OWNER'S EQUITY																					
Cash		Accounts Payable		Trayton Eli, Capital																					
<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; border-right: 1px solid red; padding: 5px;"> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; padding: 5px;">(a) 100,000</td> <td style="width: 50%; padding: 5px;">(b) 5,000</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;">(d) 1,500</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;">(e) 2,500</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;">(f) <u>8,000</u></td> </tr> <tr> <td style="padding: 5px;"><b>Bal. 83,000</b></td> <td style="padding: 5px; text-align: right;">17,000</td> </tr> </table> </td> <td style="padding: 5px;"></td> </tr> </table>	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; padding: 5px;">(a) 100,000</td> <td style="width: 50%; padding: 5px;">(b) 5,000</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;">(d) 1,500</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;">(e) 2,500</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;">(f) <u>8,000</u></td> </tr> <tr> <td style="padding: 5px;"><b>Bal. 83,000</b></td> <td style="padding: 5px; text-align: right;">17,000</td> </tr> </table>	(a) 100,000	(b) 5,000		(d) 1,500		(e) 2,500		(f) <u>8,000</u>	<b>Bal. 83,000</b>	17,000			<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; border-right: 1px solid red; padding: 5px;"> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; padding: 5px;">(e) 2,500</td> <td style="width: 50%; padding: 5px;">(c) 6,000</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;"><b>Bal. 3,500</b></td> </tr> </table> </td> <td style="padding: 5px;"></td> </tr> </table>	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; padding: 5px;">(e) 2,500</td> <td style="width: 50%; padding: 5px;">(c) 6,000</td> </tr> <tr> <td style="padding: 5px;"></td> <td style="padding: 5px;"><b>Bal. 3,500</b></td> </tr> </table>	(e) 2,500	(c) 6,000		<b>Bal. 3,500</b>			<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; border-right: 1px solid red; padding: 5px;"> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; padding: 5px;">(b) 100,000</td> </tr> </table> </td> <td style="padding: 5px;"></td> </tr> </table>	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; padding: 5px;">(b) 100,000</td> </tr> </table>	(b) 100,000	
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## SUMMARY OF ACCOUNT BALANCES

ASSETS	=	LIABILITIES	+	OWNER'S EQUITY
83,000		3,500		100,000
1,500				
8,000				
11,000				
<b>103,500</b>	<b>=</b>	<b>3,500</b>	<b>+</b>	<b>100,000</b>

## Section 2: Transactions That Affect Revenue, Expenses, and Withdrawals

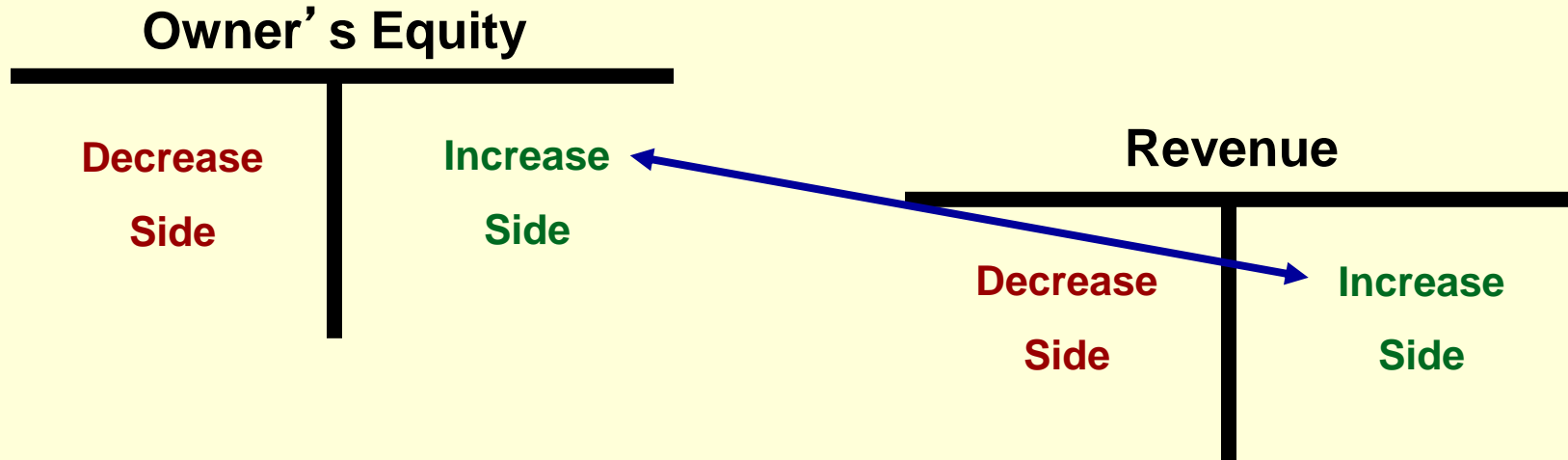
### **Learning Objective**

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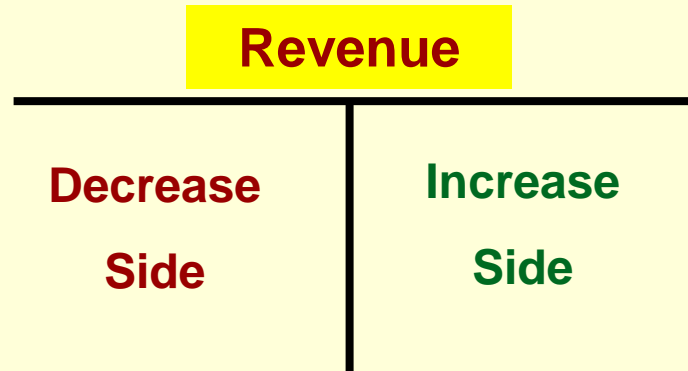
**3-4: Set up T accounts for  
revenue and expenses.**

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## T-Account for Revenue



- Revenues increase owner's equity.
- Increases in owner's equity appear on the right side of the T account.
- Therefore, increases in revenue appear on the right side of revenue T accounts.



The right side of the revenue account shows **increases** and the left side shows **decreases**.

**Decreases** in revenue accounts are rare but might occur because of corrections or transfers.

## Recording \$36,000 of Revenue from Services Sold for Cash

### Cash

Bal. 83,000

(g) 36,000

\$36,000 is entered on the left (increase) side of the asset account Cash.

### Fees Income

(g) 36,000

\$36,000 is entered on the right side of the Fees Income account.



## Recording Revenue from Services Sold on Credit

In December, Eli's Consulting Services earned \$11,000 from various charge account clients.

Analysis:

(h) The asset account, Accounts Receivable, is increased by \$11,000.

(h) The revenue account, Fees Income, is increased by \$11,000.

**Accounts Receivable**

(h) 11,000

**Fees Income**

(h) 11,000

## Receipt of Payments on Account

Charge account clients paid \$6,000, reducing the amount owed to Eli's Consulting Services.

Analysis:

- (i) The asset account, Cash, is increased by \$6,000.
- (i) The asset account, Accounts Receivable, is decreased by \$6,000.

<b>Cash</b>	
<b>(i) 6,000</b>	

<b>Accounts Receivable</b>	
	<b>(i) 6,000</b>

# Expenses

## Owner's Equity

Decrease  
Side

Increase  
Side

## Expense

Increase  
Side

Decrease  
Side

## Revenue

Decrease  
Side

Increase  
Side

- Expenses decrease owner's equity.
- Decreases in owner's equity appear on the left side of the T accounts.

## Payment of Salaries

In December, Eli's Consulting Services paid \$8,000 in salaries.

Analysis:

- (j) The asset account, Cash, is decreased by \$8,000.
- (j) The expense account, Salaries Expense, is increased by \$8,000.

Salaries Expense	Cash
(j) 8,000	(j) 8,000

## Payment of Utilities

**Eli's Consulting Services issued a check for \$650 to pay the utilities bill.**

**Analysis:**

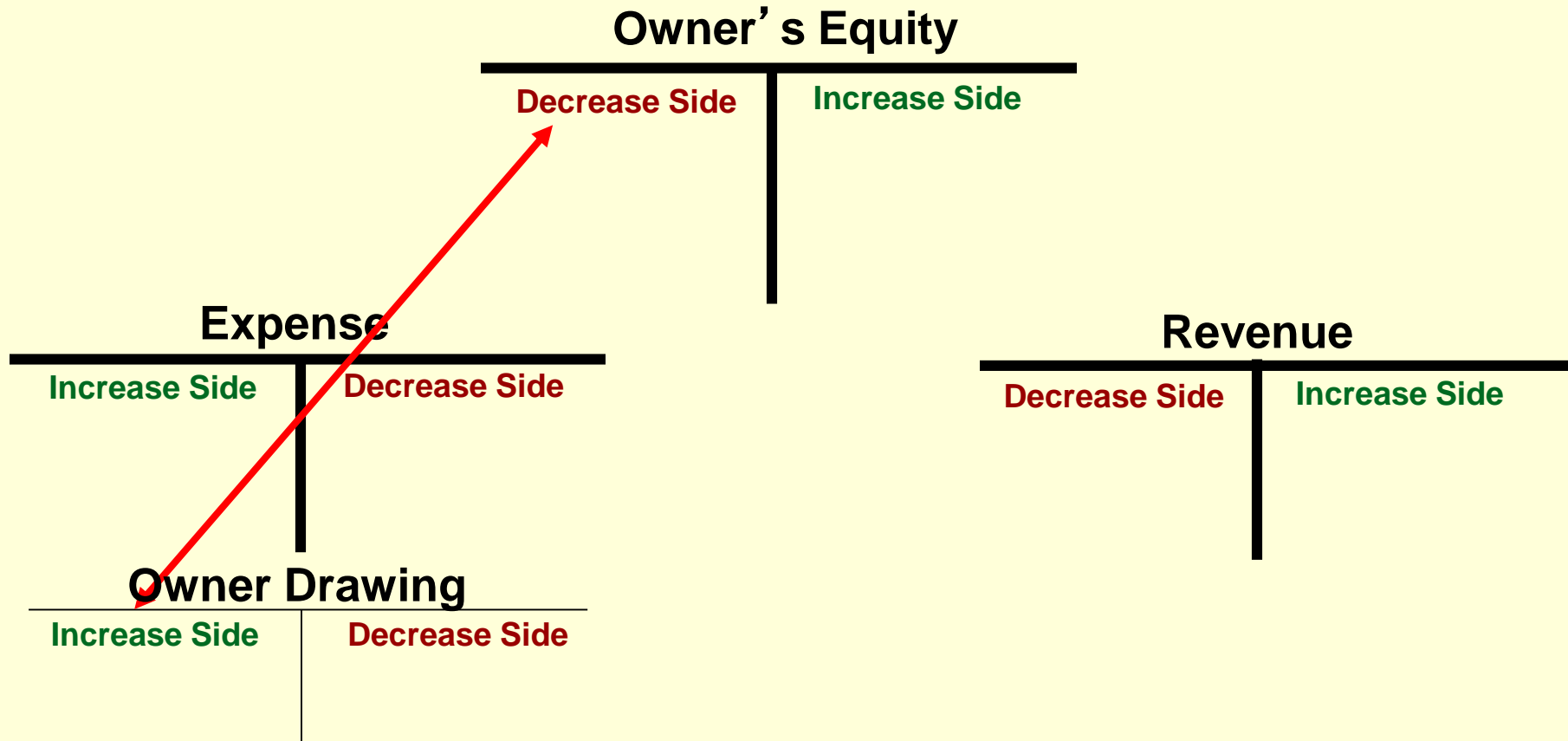
**(k) The asset account, Cash, is decreased by \$650.**

**(k) The expense account, Utilities Expense, is increased by \$650.**

<b>Utilities Expense</b>	
<b>(k)650</b>	

<b>Cash</b>	
	<b>(k) 650</b>

# Owner's Withdrawals



- Drawing decreases owner's equity.
- Decreases in owner's equity appear on the left side of the T accounts.

## The Owner Withdraws Funds

Trayton Eli wrote a check to withdraw \$5,000 cash for personal use.

Analysis:

- (I) The asset account, Cash, is *decreased* by \$5,000.
- (I) The owner's equity account, Trayton Eli, Drawing, is *increased* by \$5,000.

**Trayton Eli, Drawing**

(I) 5,000

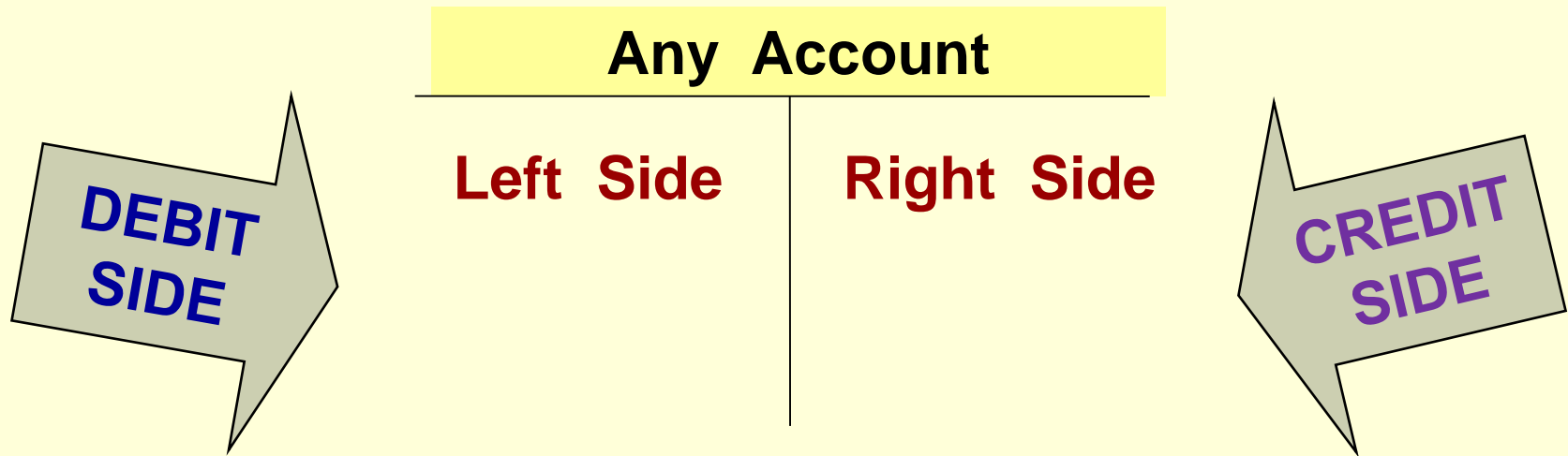
**Cash**

(I) 5,000

# The Rules of Debit and Credit

- **A debit is an entry on the left side of an account.**
- **A credit is an entry on the right side of an account.**
- **A double-entry system is an accounting system that involves recording the effects of each transaction as debits and credits in separate accounts.**
- **Every transaction in a Double entry accounting system has at least one debit and one credit.**
- **The total of the debits and credits recorded in the separate accounts must be EQUAL.**





- Accountants refer to the left side of an account as the **debit side** instead of saying the left side.
- The right side of the account is called the **credit side**.

# Rules for Debits and Credits

<p style="text-align: center;">ASSET ACCOUNTS</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; text-align: center; padding: 5px;">                     Debit + Increase Side (Normal Bal.)                 </td> <td style="width: 50%; text-align: center; padding: 5px;">                     Credit - Decrease Side                 </td> </tr> </table>	Debit + Increase Side (Normal Bal.)	Credit - Decrease Side	<p style="text-align: center;">LIABILITY ACCOUNTS</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; text-align: center; padding: 5px;">                     Debit - Decrease Side                 </td> <td style="width: 50%; text-align: center; padding: 5px;">                     Credit + Increase Side (Normal Bal.)                 </td> </tr> </table>	Debit - Decrease Side	Credit + Increase Side (Normal Bal.)	<p style="text-align: center;">OWNER'S CAPITAL ACCOUNT</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; text-align: center; padding: 5px;">                     Debit - Decrease Side                 </td> <td style="width: 50%; text-align: center; padding: 5px;">                     Credit + Increase Side (Normal Bal.)                 </td> </tr> </table>	Debit - Decrease Side	Credit + Increase Side (Normal Bal.)
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<p style="text-align: center;">OWNER'S DRAWING ACCOUNT</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; text-align: center; padding: 5px;">                     Debit + Increase Side (Normal Bal.)                 </td> <td style="width: 50%; text-align: center; padding: 5px;">                     Credit - Decrease Side                 </td> </tr> </table>	Debit + Increase Side (Normal Bal.)	Credit - Decrease Side	<p style="text-align: center;">REVENUE ACCOUNTS</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; text-align: center; padding: 5px;">                     Debit - Decrease Side                 </td> <td style="width: 50%; text-align: center; padding: 5px;">                     Credit + Increase Side (Normal Bal.)                 </td> </tr> </table>	Debit - Decrease Side	Credit + Increase Side (Normal Bal.)	<p style="text-align: center;">EXPENSE ACCOUNTS</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; text-align: center; padding: 5px;">                     Debit + Increase Side (Normal Bal.)                 </td> <td style="width: 50%; text-align: center; padding: 5px;">                     Credit - Decrease Side                 </td> </tr> </table>	Debit + Increase Side (Normal Bal.)	Credit - Decrease Side
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## Section 2: Transactions That Affect Revenue, Expenses, and Withdrawals

### Learning Objective

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**3-5: Prepare a trial balance from  
T accounts.**

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- 1. Use the proper heading to include who, what, and when information.**
- 2. List the accounts in chart of account order or in the same order as they appear in the financial statement.**
- 3. Enter the ending balance of each account in the appropriate Debit or Credit column.**
- 4. Total the Debit column.**
- 5. Total the Credit column.**
- 6. Compare the column totals. They should be equal.**

# The Trial Balance

## Eli's Consulting Services Trial Balance 12/31/2019

<u>ACCOUNT NAME:</u>	<u>DEBIT</u>	<u>CREDIT</u>
Cash	\$111,350.00	
Accounts Receivable	5,000.00	
Supplies	1,500.00	
Prepaid Rent	8,000.00	
Equipment	11,000.00	
Accounts Payable		\$3,500.00
Trayton Eli, Capital		100,000.00
Trayon Eli, Drawing	5,000.00	
Fees Income		47,000.00
Salaries Expense	8,000.00	
Utilities Expense	<u>650.00</u>	
<b>Totals</b>	<b><u>\$150,500.00</u></b>	<b><u>\$150,500.00</u></b>

# Errors

## Some common errors in a trial balance are:

- Adding trial balance columns incorrectly
- Recording only half a transaction – for example, recording a debit but not recording a credit, or vice versa
- Recording both halves of a transaction as debits or credits rather than recording one debit and one credit
- Recording the incorrect amount for a transaction
- Recording a debit for one amount and a credit for a different amount
- Mathematical errors in calculating account balances
- Forgetting to carry over an account balance to the Trial Balance

## Section 2: Transactions That Affect Revenue, Expenses, and Withdrawals

### Learning Objective

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**3-6: Prepare an income statement, a statement of owner's equity, and a balance sheet.**

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- **After the trial balance is prepared, the financial statements are prepared.**
- **Net income from the income statement is used on the statement of owner's equity.**
- **The ending balance of the *Trayton Eli, Capital* account, computed on the statement of owner's equity, is used on the balance sheet.**



**Section 2, Objective 3-6: Prepare an income statement, a statement of owner's equity, and a balance sheet**

<b>EI'S CONSULTING SERVICES</b>		
<b>Income Statement</b>		
<b>Month Ended December 31, 2019</b>		
Revenue		
Fees Income		47,000.00
Expenses		
Salaries Expense	8,000.00	
Utilities Expense	650.00	
Total Expenses		8,650.00
Net Income		<b>38,350.00</b>

<b>EI'S CONSULTING SERVICES</b>		
<b>Statement Of Owner's Equity</b>		
<b>Month Ended December 31, 2019</b>		
Trayton Eli, Capital, Dec. 1, 2019	100,000.00	
Net Income for December	38,350.00	
Less Withdrawals for December	5,000.00	
Increase in Capital		33,350.00
Trayton Eli, Capital, Dec. 31, 2019		<b>133,350.00</b>

<b>EI'S CONSULTING SERVICES</b>			
<b>Balance Sheet</b>			
<b>December 31, 2019</b>			
<b>ASSETS</b>		<b>LIABILITIES</b>	
Cash	111,350.00	Accounts Payable	3,500.00
Accounts Receivable	5,000.00		
Supplies	1,500.00		
Prepaid Rent	8,000.00		
Equipment	11,000.00		
Total Assets	<b>136,850.00</b>		
		<b>OWNER'S EQUITY</b>	
		Trayton Eli, Capital	133,350.00
		Total Liabilities and Owner's Equity	<b>136,850.00</b>

## **Section 2: Transactions That Affect Revenue, Expenses, and Withdrawals**

### **Learning Objective**

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**3-7: Develop a chart of accounts**

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- **Each account has a number and a name.**
- **The Balance Sheet accounts are listed first, followed by the Statement of Owner's Equity accounts, ending with the income statement accounts.**
- **The account number is assigned based on the type of account.**
- **Each account should have a number assigned to its title (name)**
- **Balance Sheet accounts are listed before income statement accounts.**

## Section 2, Objective 3-7: Develop a chart of accounts

<b>Eli's Consulting Services Chart of Accounts</b>	
<b>Account Number</b>	<b>Account Name</b>
<b>Balance Sheet Accounts</b>	
<b>100–199</b>	<b>ASSETS</b>
101	Cash
111	Accounts Receivable
121	Supplies
137	Prepaid Rent
141	Equipment
<b>200–299</b>	<b>LIABILITIES</b>
202	Accounts Payable
<b>300–399</b>	<b>OWNER'S EQUITY</b>
301	Trayton Eli, Capital
<b>Statement of Owner's Equity Account</b>	
302	Trayton Eli, Drawing
<b>Income Statement Accounts</b>	
<b>400–499</b>	<b>REVENUE</b>
401	Fees Income
<b>500–599</b>	<b>EXPENSES</b>
511	Salaries Expense
514	Utilities Expense

## Permanent and Temporary Accounts

**A permanent account is an account that is kept open from one accounting period to the next.**

**A temporary account is an account whose balance is transferred to another account at the end of an accounting period. A temporary account is “zeroed out” at the end of the accounting period.**

# Thank You

for using

***College Accounting:  
A Contemporary Approach  
4th Edition***

**Haddock • Price • Farina**