**Name \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_** Accounting - Chapter 2

Starting a Proprietorship -Changes that AffectOwner’s Equity

# **2-1 How Transactions Change Owner's Equity in an Accounting Equation**

# A. Revenue Transactions

**1. Received Cash from Sales**

a. sale of goods or services = revenue

b. revenue – an increase in owner’s equity resulting from the

operating of a business.

c. When cash is received from a sale, assets & owner’s equity

are increased.

Transaction 6 - August 12. Received cash from sales, $325.00

1) Cash increases

2) BT Capital increases

**2. Sold Services on Account**

a. Sale on Account – cash is received from a sale or an

account is charged.

b. The Business

1) Encore Music has contracts with 2 daycare centers to

provide music lessons to the children at the centers.

2) These centers are allowed to pay the cash at a later

date (services are sold on account).

3) All *other* customers must pay cash at the time of the lessons.

c. When services are sold on account**, Accounts Receivable**

**(new asset account)** is increased by the amount of cash

received.

d. Revenue in “Accounts Receivable” should be recorded *at*

*the time of sale*, regardless when payment is made.

e. Owner’s Equity account is also increased because it is like

an investment.

f. CONCEPT: *Realization of Revenue* – When revenue is

recorded at the time goods and services are sold.

Transaction 7 – August 12, Sold services on account to Kids Time, $200.00

g. Accounts Receivable – Kids Time is increased

h. BT Capital is increased

**B. Paid Cash for Expenses**

1. Paying for goods or services needed to operate a business

results in a decrease in owner’s equity.

2. When cash is paid for expenses, the business has less cash.

Transaction 8 – August 12. Paid cash for rent, $250.00

Transaction 9 – August 12. Paid cash for phone bill, $45.00

a. Cash is decreased

b. BT Capital is decreased

**C. Transactions**

**1. Received Cash on Account**

a. Company receives cash from a customer for a prior sale.

Transaction 10 – August 12, Received cash on account from Kids Time, $100.00

1) Cash Increases

2) Accounts Receivable Decreases

**2. Paid Cash to Owner for Personal Use – Not an expense.**

a. Withdrawals - Assets taken out of a business for the

owner’s personal use. (drawing)

b. Decreases owner’s equity.

c. Owner may withdraw any kind of asset, but usually they

withdraw cash.

Transaction 11 – August 12, paid cash to owner for personal use, $100.00

1) Asset account (Cash) is decreased

2) BT Capital is decreased

d. A decrease in owner’s equity because of a withdrawal is

not a result of the normal operations of a business.

Therefore, a **withdrawal is not an expense.**

3. Summary of Changes in Owner’s Equity

|  |  |  |
| --- | --- | --- |
| **Transaction**  **Number** | **Kind of Transaction** | **Change in Owner’s Equity** |
| 6 | Revenue (cash) | + 325.00 |
| 7 | Revenue (on account-accounts receivable) | +200.00 |
| 8 | Expense (rent) | -250.00 |
| 9 | Expense (telephone) | -45.00 |
| 11 | Withdrawal | -100.00 |
|  | **Net change in Owner’s Equity** | **+130.00** |

# **2-2 Reporting a Changed Accounting Equation on a Balance Sheet**

A. Update the old balance sheet figures with the new figures.

B. When one side of the sheet is longer than the other side, an

adjustment must be made in order to have the totals of the two sides

on the same line. (leave a line blank) pg. 30

C. Balance sheets are often prepared the last day of each month.

D. Balance sheets help business owners and managers make business

decisions.

Accounting

Ch. 2 Transactions

* Transaction 6

August 12, received $325.00 cash from sales.

**+Cash +Capital**

* Transaction 7

August 12, sold $200.00 services on account to Kids Time.

***-no cash received***

**+Accounts Receivable +Capital**

*Concept of realization of revenue*

* Transaction 8

August 12, paid $250.00 cash for rent.

**- Cash - Capital**

* Transaction 9

August 12, paid $45.00 cash for telephone bill

**- Cash - Capital**

* Transaction 10

August 12, received $100.00 cash on account from Kids Time.

**+ Cash - Accounts Receivable**

* Transaction 11

August 12, paid $100.00 cash to owner for personal use.

- **Cash - Capital**