

3 Analyzing Transactions into Debit and Credit Parts

AFTER STUDYING CHAPTER 3, YOU WILL BE ABLE TO:

1. Define accounting terms related to analyzing transactions into debit and credit parts.
2. Identify accounting practices related to analyzing transactions into debit and credit parts.
3. Use T accounts to analyze transactions showing which accounts are debited or credited for each transaction.
4. Analyze how transactions to set up a business affect accounts.
5. Analyze how transactions affect owner's equity accounts.

TERMS PREVIEW

T account

debit

credit

normal balance

chart of accounts

ANALYZING THE ACCOUNTING EQUATION

Even though the effects of transactions *can* be recorded in an accounting equation, the procedure is not practical in an actual accounting system. The number of accounts used by most businesses would make the accounting equation cumbersome to use as a major financial record. Therefore, a separate record is commonly used for each account. The accounting equation can be represented as a T, as shown.

Assets	=	Liabilities	+	Owner's Equity
Left side				Right side

The values of all things owned (assets) are on the left side of the accounting equation. The values of all equities or claims against the assets (liabilities and owner's equity) are on the right side of the accounting equation. The total of amounts on the left side of the accounting equation must always equal the total of amounts on the right side. Therefore, the total of all assets on the left side of the accounting equation must always equal the total of all liabilities and owner's equity on the right side.

ACCOUNTING IN YOUR CAREER

ADDING ACCOUNTS

John Robbin, the owner of Robbin's Auto Service, has requested a meeting with Diane Endo, his accounting assistant, to discuss changes in the business.

Diane Endo: You asked to see me, John.
What's up?

John Robbin: Diane, you've been my accounting assistant for nine months, and I've been impressed with what you've learned and how well you journalize all the company's transactions.

Diane Endo: Thanks, John. It's been fun to learn and I enjoy working for this company.

John Robbin: Now I need your creative thinking. More and more people are servicing their own cars, so I've been thinking about branching out to sell auto parts.

Diane Endo: Sounds like a good idea. What do you want me to do?

John Robbin: I'd like you to recommend changes to the chart of accounts.

John Robbin: I'd like you to recommend changes to the chart.

Diane Endo: I've got some thoughts already. What do you want to accomplish?

John Robbin: I'd like you to read this information?

Diane Endo: When do you need this information?

Diane Endo: When do you need this information?

John Robbin: Well, today is Monday. Can you have it ready by Wednesday? I want to move fast on this.

Critical Thinking:

- Critical Thinking:**
1. What kinds of new accounts should Diane Endo recommend?
 2. Should she recommend any changes to the numbering system of the chart of accounts?



3-1 Using T Accounts

ACCOUNTS

Assets	=	Liabilities	+	Owner's Equity
Left side		Right side		
T Account				
Left side DEBIT SIDE		Right side CREDIT SIDE		

A record summarizing all the information pertaining to a single item in the accounting equation is known as an account. Transactions change the balances of accounts in the accounting equation. Accounting transactions must be analyzed to determine how account balances are changed. An accounting device used to analyze transactions is called a **T account**.

There are special names for amounts recorded on the left and right sides of a T account. An amount recorded on the left side is called a **debit**. An amount recorded on the right side is called a **credit**. The words *debit* and *credit* come from the Latin and Italian words *debere* and *credere*. Common abbreviations are *dr.* for debit and *cr.* for credit.

ACCOUNT BALANCES

Assets		=	Liabilities + Owner's Equity	
Any Asset			Any Liability	
Debit NORMAL BALANCE	Credit		Debit	Credit NORMAL BALANCE
			Owner's Capital Account	
			Debit	Credit NORMAL BALANCE

The side of the account that is increased is called the **normal balance**. The process of increasing or decreasing account balances is discussed on the next page. Assets are on the left side of the accounting equation, and asset accounts have normal debit balances (left side).

Liabilities are on the right side of the accounting equation, and liability accounts have normal credit balances (right side). The owner's capital account is on the right side of the accounting equation and has a normal credit balance (right side).

INCREASES AND DECREASES IN ACCOUNTS

Assets		=	Liabilities	+	Owner's Equity
Any Asset			Any Liability		
Debit	Credit		Debit	Credit	
NORMAL BALANCE				NORMAL BALANCE	
↑	↓		↓	↑	
			Owner's Capital Account		
			Debit	Credit	
				NORMAL BALANCE	
			↓	↑	

The sides of a T account are used to show increases and decreases in account balances.

Two basic accounting rules regulate increases and decreases of account balances. (1) Account balances increase on the normal balance side of an account. (2) Account balances decrease on the side opposite the normal balance side of an account.

Asset accounts have normal debit balances;

therefore, asset accounts increase on the debit side and decrease on the credit side. Liability accounts have normal credit balances; therefore, liability accounts increase on the credit side and decrease on the debit side. The owner's capital account has a normal credit balance; therefore, the capital account increases on the credit side and decreases on the debit side.

DINING OUT WITH COMPUTERS

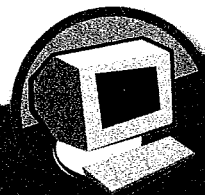
Next time you order a taco—think technology. That's right, technology is changing the way restaurants do business. Computers are widely used to enter orders, generate guest checks, and print receipts. Computers also track the menu items that diners order—how many of each item is served each day, what time of day it is ordered, and what other items are ordered along with it.

The technology makes it possible for restaurant managers to predict how much of each food item to order, how much to prepare on a given day,

and when to start cooking. Computer software programs also help managers plan their staffing needs based on trends developed from historical data.

Hand-held computers are used by servers in some restaurants to transmit information to the kitchen, where it is printed for the chef. This technology can reduce the time diners sit at a table. That translates into more diners served and more revenue for the restaurant.

Remember, technology is all around, even when you order that taco.



**TECHNOLOGY
FOR BUSINESS**

TERMS REVIEW

T account
debit
credit
normal balance

AUDIT YOUR UNDERSTANDING

1. Draw the accounting equation on a T account.
2. What are the two accounting rules that regulate increases and decreases of account balances?

WORK TOGETHER

Determining the normal balance, increase, and decrease sides for accounts

Write the answers to the following problems in the *Working Papers*. Your instructor will guide you through the following example.

Cash

Accounts Receivable—Christine Kelly

Supplies

Prepaid Insurance

Accounts Payable—Miller Supplies

Accounts Payable—Wayne Office Supplies

Jeff Dixon, Capital

For each of the accounts, complete the following:

3. Prepare a T account.
4. Label the debit and credit sides.
5. Label each side of the T account using the following labels:
 - a. Normal balance
 - b. Increase side
 - c. Decrease side

ON YOUR OWN

Determining the normal balance, increase, and decrease sides for accounts

Write the answers to the following problems in the *Working Papers*. Work these problems independently.

Cash

Accounts Receivable—Brian Lee

Supplies

Prepaid Insurance

Accounts Payable—Golf Tees

Vickie Haskins, Capital

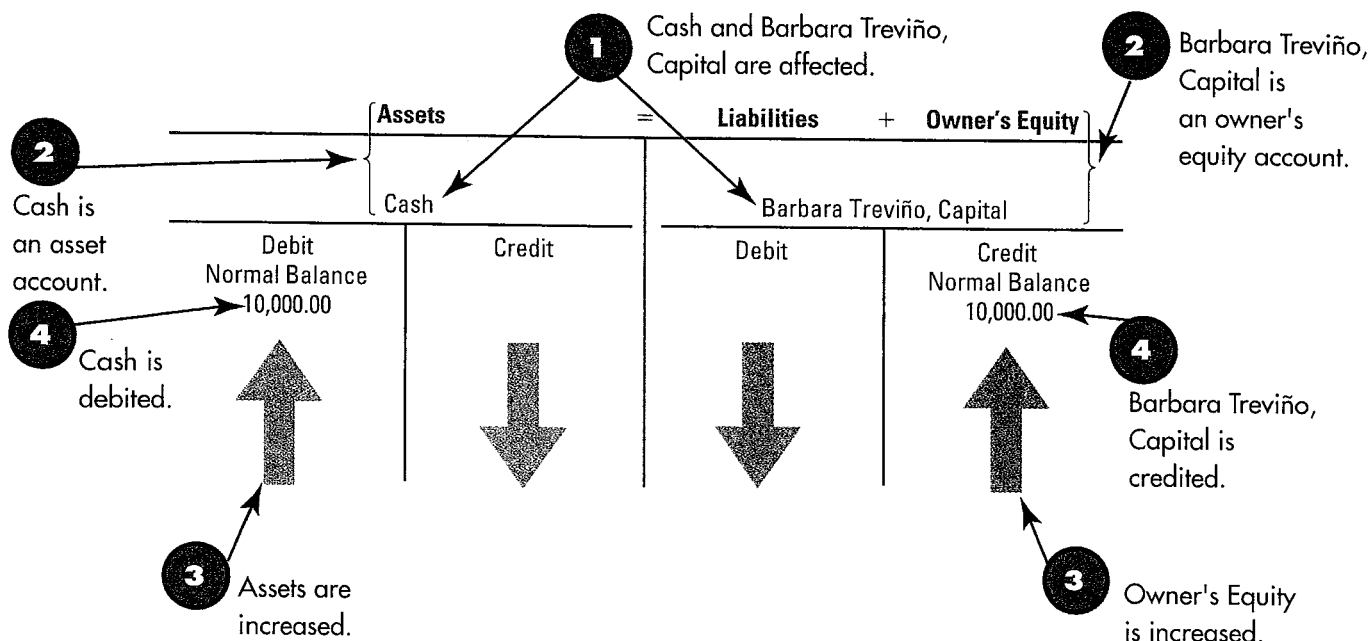
For each of the accounts, complete the following:

6. Prepare a T account.
7. Label the debit and credit sides.
8. Label each side of the T account using the following labels:
 - a. Normal balance
 - b. Increase side
 - c. Decrease side

3-2

Analyzing How Transactions Affect Accounts

RECEIVED CASH FROM OWNER AS AN INVESTMENT



August 1. Received cash from owner as an investment, \$10,000.00.

The effect of this transaction is shown in the illustration. Before a transaction is recorded in the records of a business, the information is analyzed to determine which accounts are changed and how. Each transaction changes the balances of at least two accounts. A list of accounts used

by a business is called a **chart of accounts**. The chart of accounts for Encore Music is found on page 3.

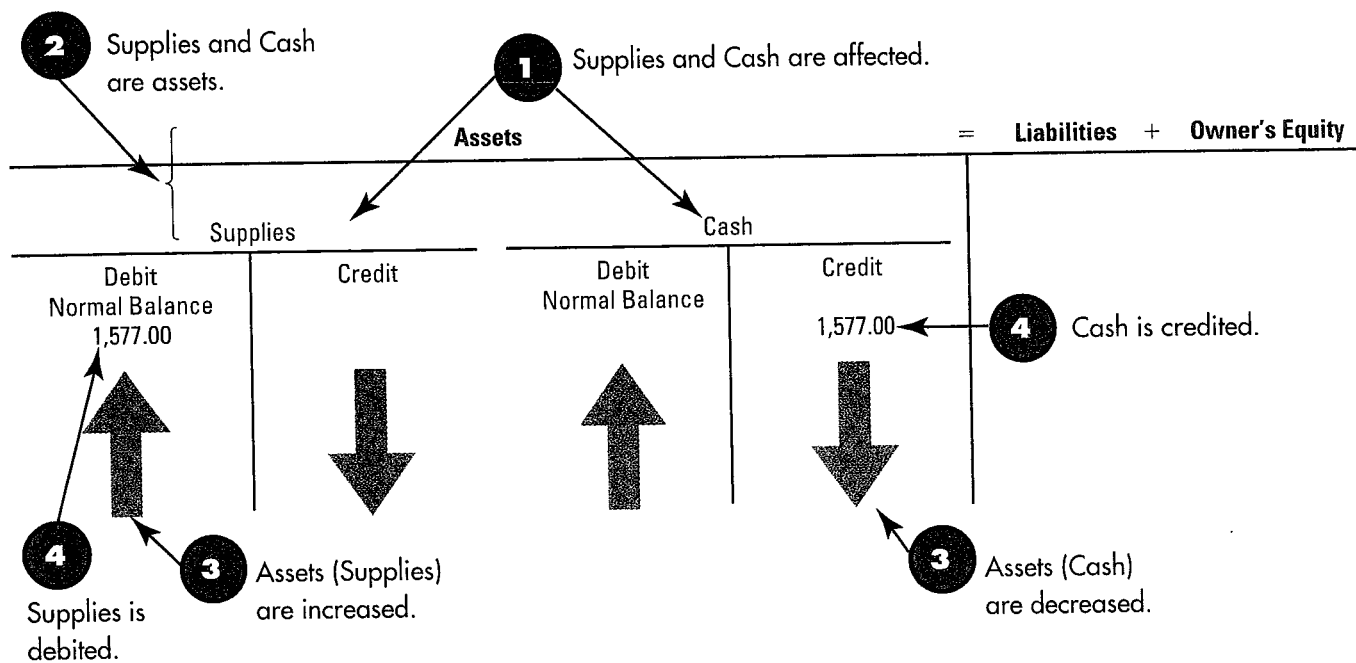
Four questions are used in analyzing a transaction into its debit and credit parts. Debits equal credits for each transaction. In addition, after a transaction is recorded, total debits must equal total credits.

S Questions for analyzing a transaction into its debit and credit parts

STEP S

- Which accounts are affected?
Cash and Barbara Treviño, Capital
- How is each account classified?
Cash is an asset account. Barbara Treviño, Capital is an owner's equity account.
- How is each classification changed?
Assets are increased. Owner's equity is increased.
- How is each amount entered in the accounts?
Assets increase on the debit side. Therefore, the asset account, Cash, is debited. Owner's equity accounts increase on the credit side. Therefore, the owner's equity account, Barbara Treviño, Capital, is credited.

PAID CASH FOR SUPPLIES



August 3. Paid cash for supplies, \$1,577.00.

The effect of this transaction on the accounting equation is shown in the illustration. In this transaction, two asset accounts are changed. One asset, cash, has been exchanged for another asset, supplies. The asset account, Cash, is decreased by \$1,577.00, the amount of cash paid out. This decrease is on the left side of the accounting equation. The asset account, Supplies, is increased by \$1,577.00, the amount of supplies bought. This increase is also on the left side of the accounting equation.

The two changes are both on the left side of the accounting equation. When changes are made on only one side of the accounting

equation, the equation must still be in balance. Therefore, if one account is increased, another account on the same side of the equation must be decreased.

As you have seen, transactions must be carefully analyzed. It must be determined if a transaction affects accounts from both sides of the accounting equation. Or a transaction may affect accounts that are on the same side of the accounting equation, as is true in this example. A common error is to assume that every transaction must affect accounts from both sides of the accounting equation.

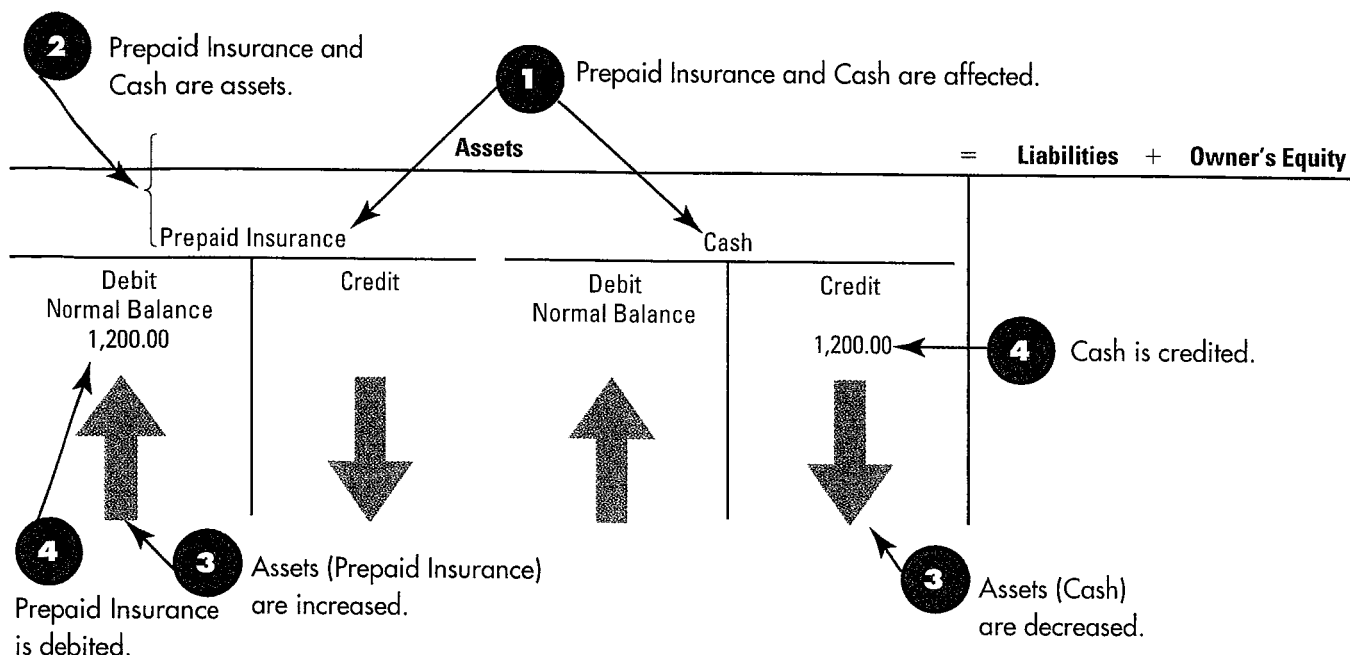
The same four questions are used every time a transaction is analyzed.

S Questions for analyzing a transaction into its debit and credit parts

**T
E
P
S**

1. Which accounts are affected?
Supplies and Cash
2. How is each account classified?
Supplies is an asset account. Cash is an asset account.
3. How is each classification changed?
Assets (Supplies) are increased and assets (Cash) are decreased.
4. How is each amount entered in the accounts?
Assets increase on the debit side. Therefore, the asset account, Supplies, is debited. Assets decrease on the credit side. Therefore, the asset account, Cash, is credited.

PAID CASH FOR INSURANCE



August 4. Paid cash for insurance, \$1,200.00.

Paying cash for insurance is very similar to paying cash for supplies. One asset is increased and one asset is decreased.

The effect of this transaction on the accounting equation is shown in the illustration. In this transaction, two assets are changed. One asset, cash, has been exchanged for another asset, prepaid insurance. The asset account, Cash, is decreased by \$1,200.00, the amount of cash paid

out. This decrease is on the left side of the accounting equation. The asset account, Prepaid Insurance, is increased by \$1,200.00, the amount of insurance bought. This increase is also on the left side of the accounting equation.

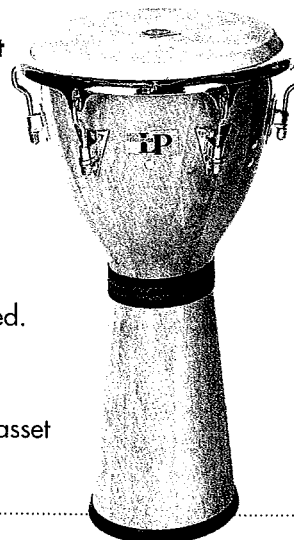
F
Y
L

T accounts get their names from the arrangement of the lines making up the account. The horizontal line on top of the centered vertical line together look like a capital T.

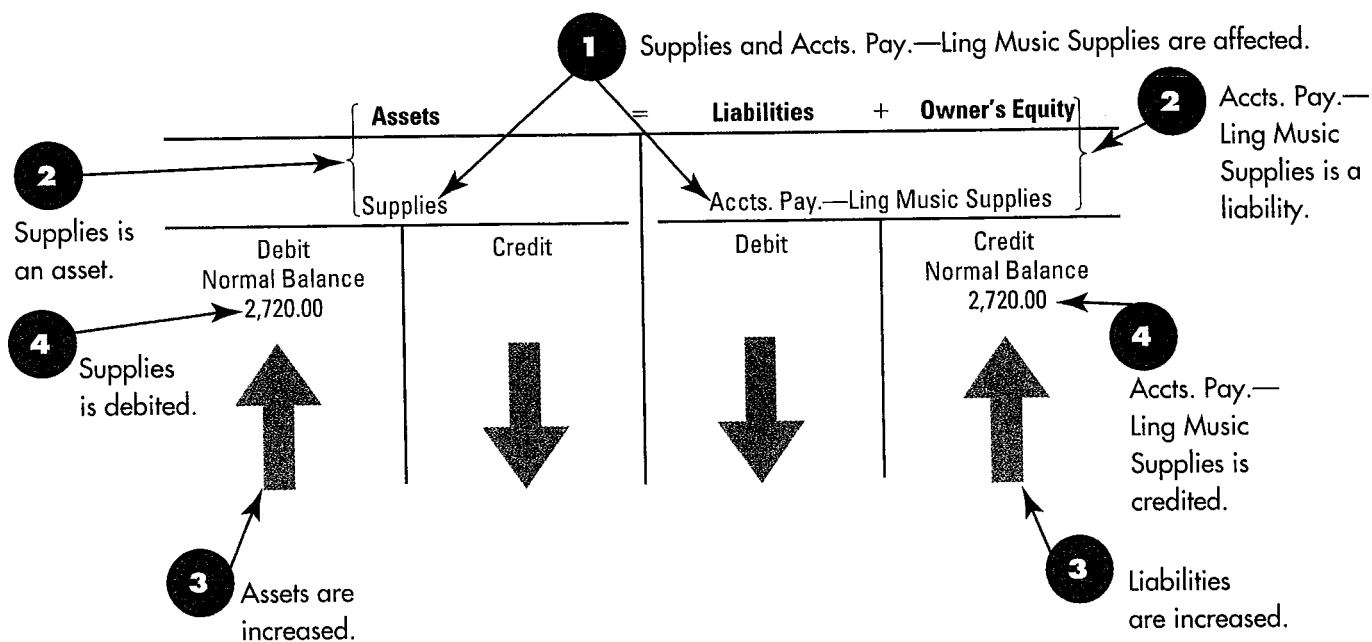
S Questions for analyzing a transaction into its debit and credit parts

T
E
P
S

- Which accounts are affected?
Prepaid Insurance and Cash
- How is each account classified?
Prepaid Insurance is an asset account. Cash is an asset account.
- How is each classification changed?
Assets (Prepaid Insurance) are increased and assets (Cash) are decreased.
- How is each amount entered in the accounts?
Assets increase on the debit side. Therefore, the asset account, Prepaid Insurance, is debited. Assets decrease on the credit side. Therefore, the asset account, Cash, is credited.



BOUGHT SUPPLIES ON ACCOUNT



August 7. Bought supplies on account from Ling Music Supplies, \$2,720.00.

The effect of this transaction on the accounting equation is shown in the illustration. In this transaction, one asset and one liability are changed. The asset account, Supplies, is increased by \$2,720.00, the amount of supplies bought. This increase is on the left side of the

accounting equation. Ling Music Supplies will have a claim against some of Encore Music's assets until Encore Music pays for the supplies bought. Therefore, Accounts Payable—Ling Music Supplies is a liability account. The liability account, Accounts Payable—Ling Music Supplies, is increased by \$2,720.00, the amount owed for the supplies. This increase is on the right side of the accounting equation.

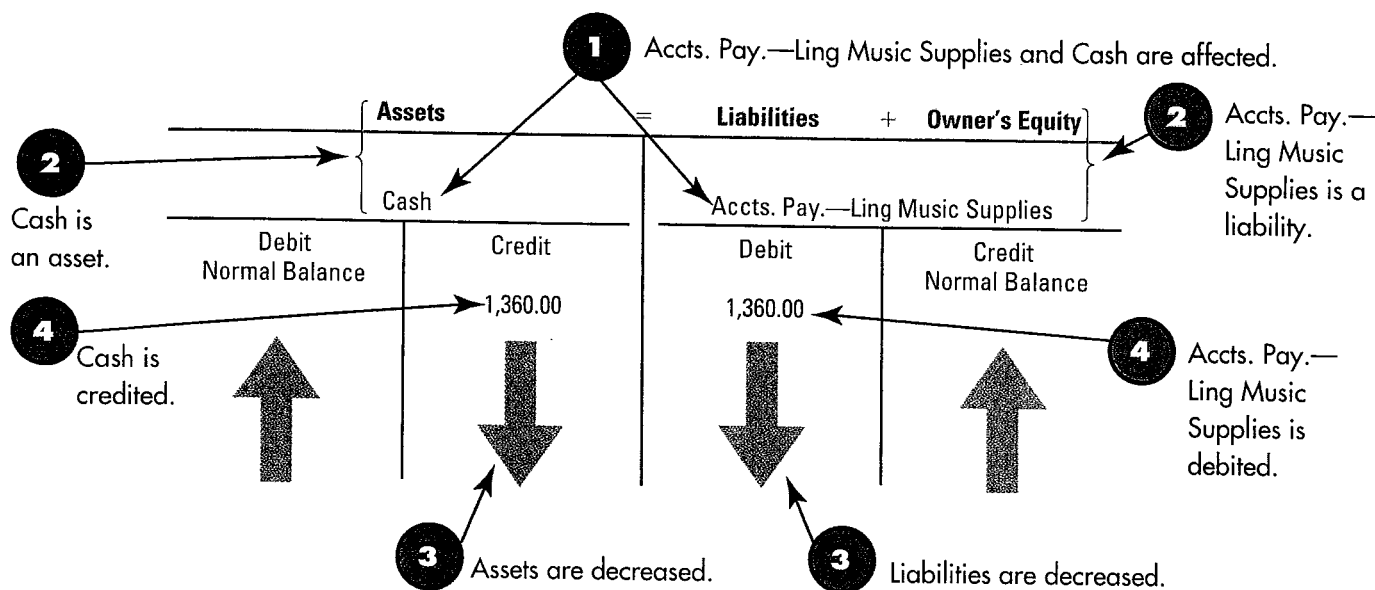
STEPS Questions for analyzing a transaction into its debit and credit parts

- Which accounts are affected?
Supplies and Accounts Payable—Ling Music Supplies
- How is each account classified?
Supplies is an asset account. Accounts Payable—Ling Music Supplies is a liability account.
- How is each classification changed?
Assets are increased. Liabilities are increased.
- How is each amount entered in the accounts?
Assets increase on the debit side. Therefore, the asset account, Supplies, is debited. Liabilities increase on the credit side. Therefore, the liability account, Accounts Payable—Ling Music Supplies, is credited.

FYI

Paying cash for insurance and buying supplies for cash are examples of transactions that affect only one side of the accounting equation. All the accounts involved in these transactions are assets.

PAID CASH ON ACCOUNT



August 11. Paid cash on account to Ling Music Supplies, \$1,360.00.

The effect of this transaction on the accounting equation is shown in the illustration. In this transaction, one asset and one liability are changed. The asset account, **Cash**, is decreased by \$1,360.00, the amount of cash paid out. This

decrease is on the left side of the accounting equation. After this payment, Encore Music owes less money to Ling Music Supplies. Therefore, the liability account, **Accounts Payable—Ling Music Supplies**, is decreased by \$1,360.00, the amount paid on account. The decrease is on the right side of the accounting equation.

S Questions for analyzing a transaction into its debit and credit parts

- 1.** Which accounts are affected?
Accounts Payable—Ling Music Supplies and Cash
- 2.** How is each account classified?
Accounts Payable—Ling Music Supplies is a liability account. Cash is an asset account.
- 3.** How is each classification changed?
Liabilities are decreased. Assets are decreased.
- 4.** How is each amount entered in the accounts?
Liabilities decrease on the debit side. Therefore, the liability account, Accounts Payable—Ling Music Supplies, is debited. Assets decrease on the credit side. Therefore, the asset account, Cash, is credited.

F.Y.I.

A chart of accounts is sometimes referred to by its initials COA. Many accounting terms are often abbreviated or referred to by initials. For example, accounts payable is sometimes referred to as A/P.

REMEMBER

When you decrease an account balance, record the decrease on the side opposite the normal balance side of the account. The side opposite the normal balance side can be on the left or the right depending on the type of account.

TERM REVIEW

chart of accounts

AUDIT YOUR UNDERSTANDING

1. State the four questions used to analyze a transaction.
2. What two accounts are affected when a business pays cash for supplies?

WORK TOGETHER

T accounts are given in the *Working Papers*. Your instructor will guide you through the following examples. Kathy Bergum owns Bergum Services. Bergum Services uses the following accounts. Some of the accounts will be explained in Lesson 3-3.

Cash	Supplies	Kathy Bergum, Drawing	Rent Expense
Accts. Rec.—Sam Erickson	Prepaid Insurance	Sales	
Accts. Pay.—Bales Supplies	Kathy Bergum, Capital	Advertising Expense	

Transactions: Apr. 1. Received cash from owner as an investment, \$5,000.00.

2. Paid cash for supplies, \$50.00.

5. Paid cash for insurance, \$75.00.

6. Bought supplies on account from Bales Supplies, \$100.00.

9. Paid cash on account to Bales Supplies, \$50.00.

3. For each transaction write on T accounts the account titles of the two accounts affected.
4. Write the debit or credit amount in each T account to show the transaction's effect.

ON YOUR OWN

Analyzing a transaction into its debit and credit parts

T accounts are given in the *Working Papers*. Work these problems independently. Jens Puckett owns Jens Accounting Service. Jens Accounting Service uses the following accounts. Some of the accounts will be explained in Lesson 3-3.

Cash	Supplies	Jens Puckett, Drawing	Utilities Expense
Accts. Rec.—King Company	Prepaid Insurance	Sales	
Accts. Pay.—Computer Supply	Jens Puckett, Capital	Miscellaneous Expense	

Transactions: Sept. 1. Received cash from owner as an investment, \$3,000.00.

4. Paid cash for insurance, \$100.00.

5. Paid cash for supplies, \$90.00.

6. Bought supplies on account from Computer Supply, \$200.00.

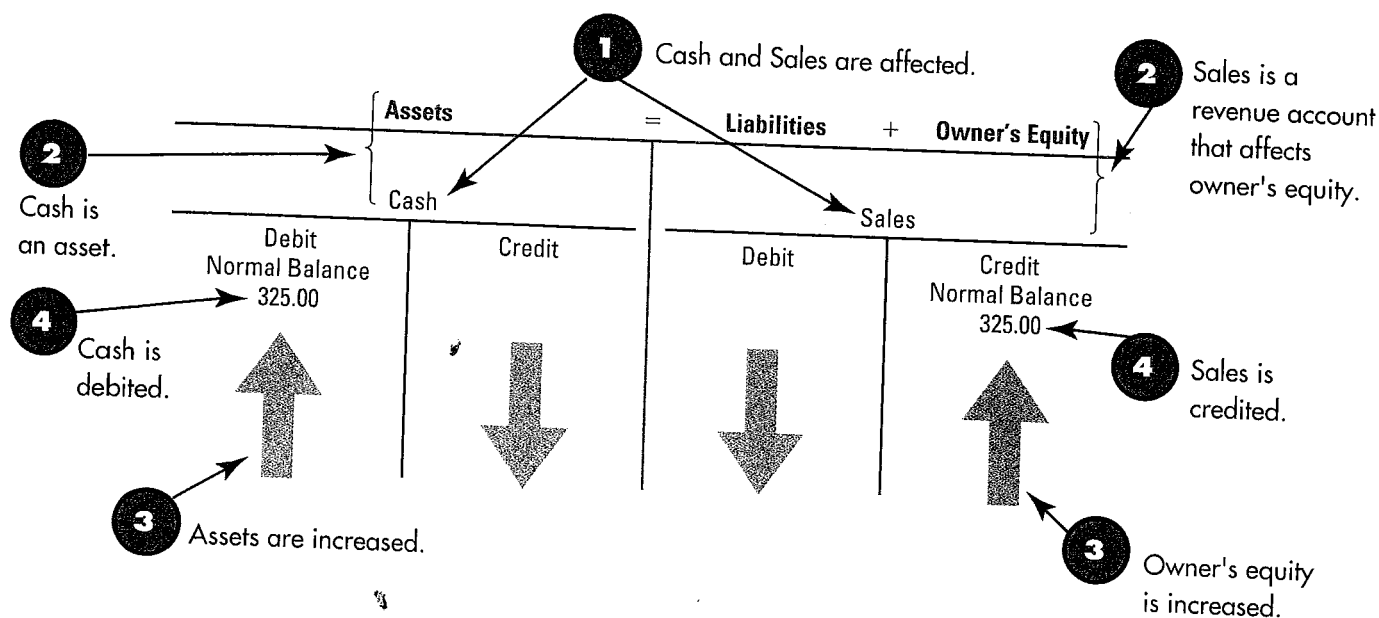
11. Paid cash on account to Computer Supply, \$150.00.

5. For each transaction write on T accounts the account titles of the two accounts affected.
6. Write the debit or credit amount in each T account to show the transaction's effect.

3-3

Analyzing How Transactions Affect Owner's Equity Accounts

RECEIVED CASH FROM SALES



August 12. Received cash from sales, \$325.00.

Revenue increases owner's equity. The increases from revenue could be recorded directly in the owner's capital account. However, to avoid a capital account with a large number of entries and to summarize revenue information separately from the other records, Encore Music uses a separate revenue account titled Sales.

The owner's capital account has a normal credit balance. Increases in the owner's capital

account are shown as credits. Because revenue increases owner's equity, increases in revenue are recorded as credits. A revenue account has a normal credit balance.

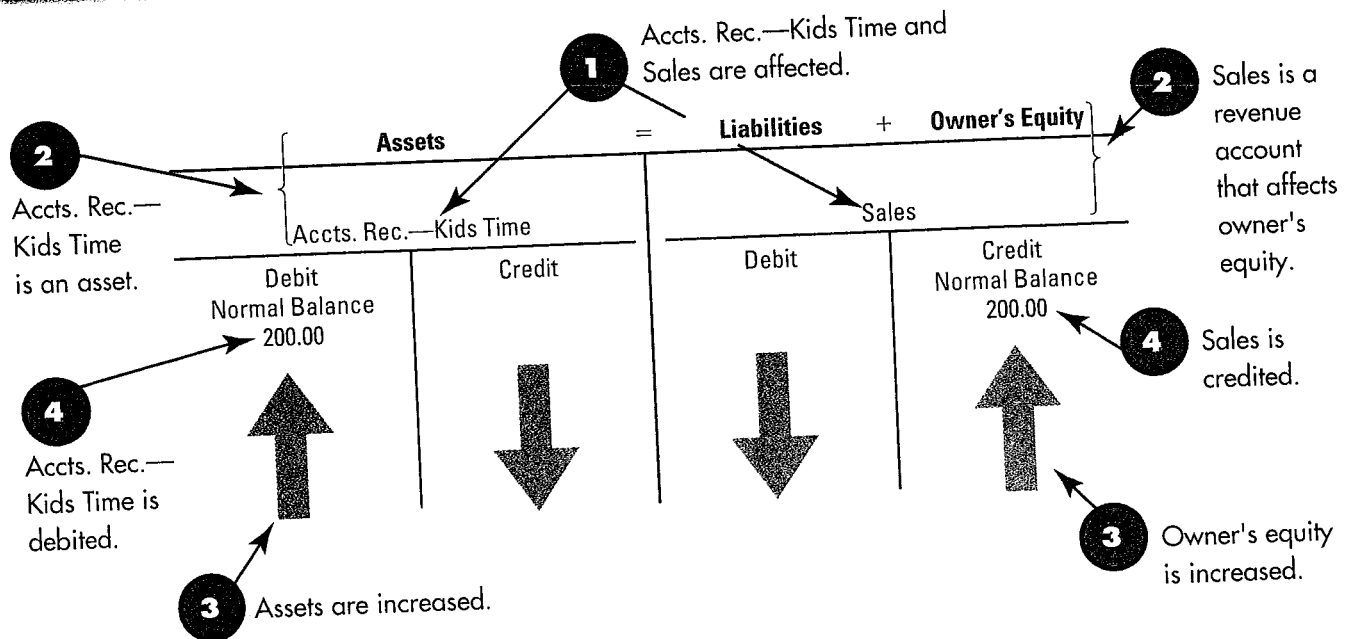
FACT

The Small Business Administration (SBA) offers two major types of loans to small businesses. One type of loan is made by private lending institutions. Another type of loan is made directly by the SBA.

STEPS Questions for analyzing a transaction into its debit and credit parts

- Which accounts are affected?
Cash and Sales
- How is each account classified?
Cash is an asset account. Sales is a revenue account that affects owner's equity.
- How is each classification changed?
Assets are increased. Owner's equity is increased.
- How is each amount entered in the accounts?
Assets increase on the debit side. Therefore, the asset account, Cash, is debited. Owner's equity accounts increase on the credit side. Revenue increases owner's equity. Therefore, the revenue account, Sales, is credited.

SOLD SERVICES ON ACCOUNT



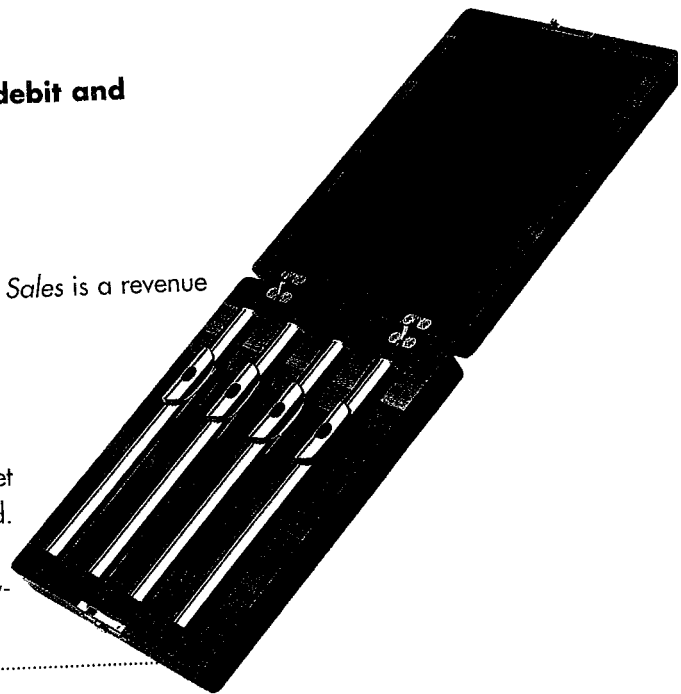
August 12. Sold services on account to Kids Time, \$200.00.

The analysis for selling services on account is similar to that for selling services for cash. The only difference is that cash is not received at this

time; therefore, the cash account is not affected by the transaction. Instead, this transaction increases an accounts receivable account. The same four questions are used to analyze this transaction into its debit and credit parts.

STEPS Questions for analyzing a transaction into its debit and credit parts

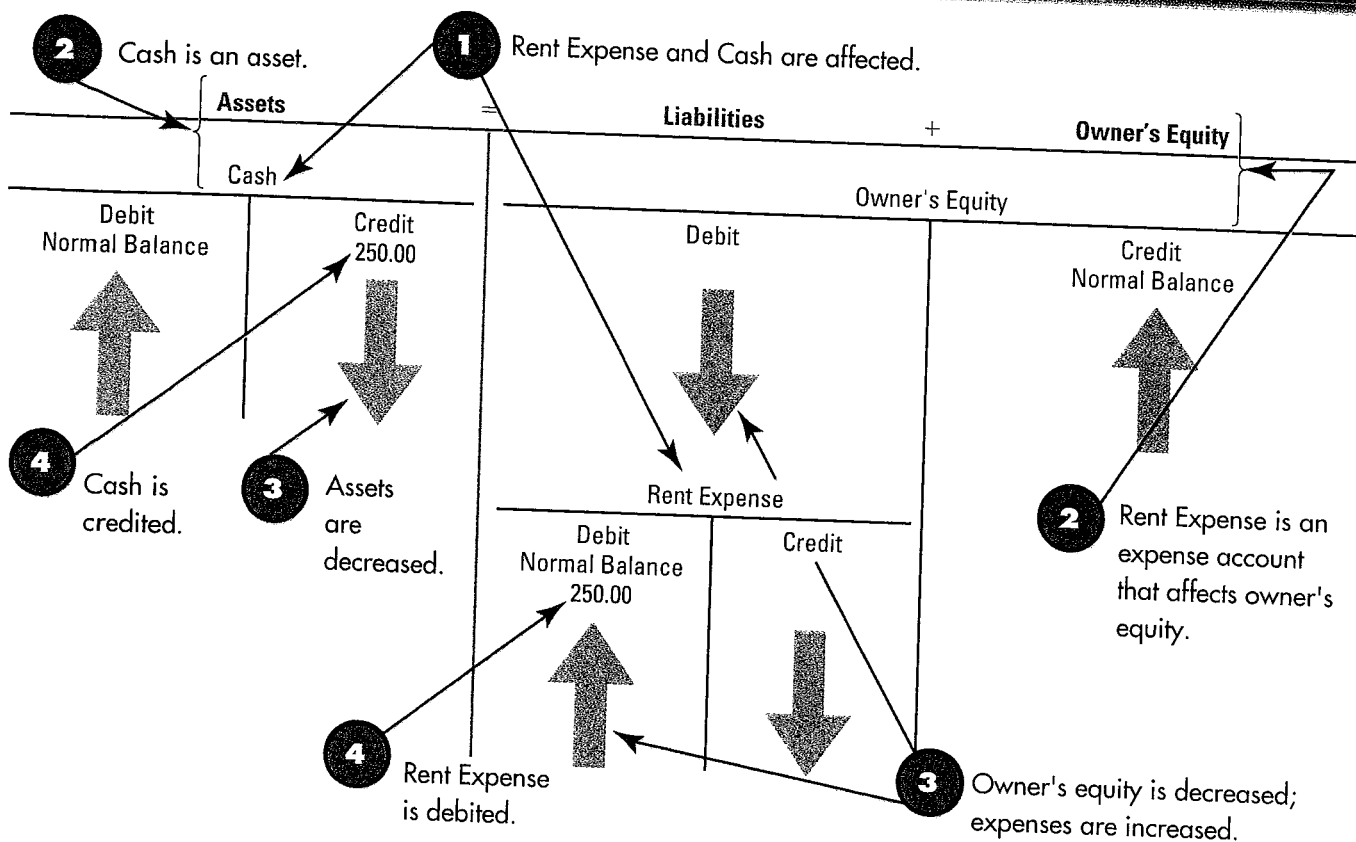
- Which accounts are affected?
Accounts Receivable—Kids Time and Sales
- How is each account classified?
Accounts Receivable—Kids Time is an asset account. Sales is a revenue account that affects owner's equity.
- How is each classification changed?
Assets are increased. Owner's equity is increased.
- How is each amount entered in the accounts?
Assets increase on the debit side. Therefore, the asset account, Accounts Receivable—Kids Time, is debited. Owner's equity accounts increase on the credit side. Revenue increases owner's equity. Therefore, the revenue account, Sales, is credited.



REMEMBER

Owner's equity is recorded on the right side of the accounting equation. The right side of a T account is the credit side. Therefore, owner's equity has a normal credit balance.

PAID CASH FOR AN EXPENSE



August 12. Paid cash for rent, \$250.00.

Expenses decrease owner's equity. The decreases from expenses could be recorded directly in the owner's capital account. However, to avoid a capital account with a large number of entries and to summarize expense information separately from the other records, Encore Music uses separate expense accounts.

The titles of Encore Music's expense accounts are shown on its chart of accounts. The

expense account, Rent Expense, is used to record all payments for rent.

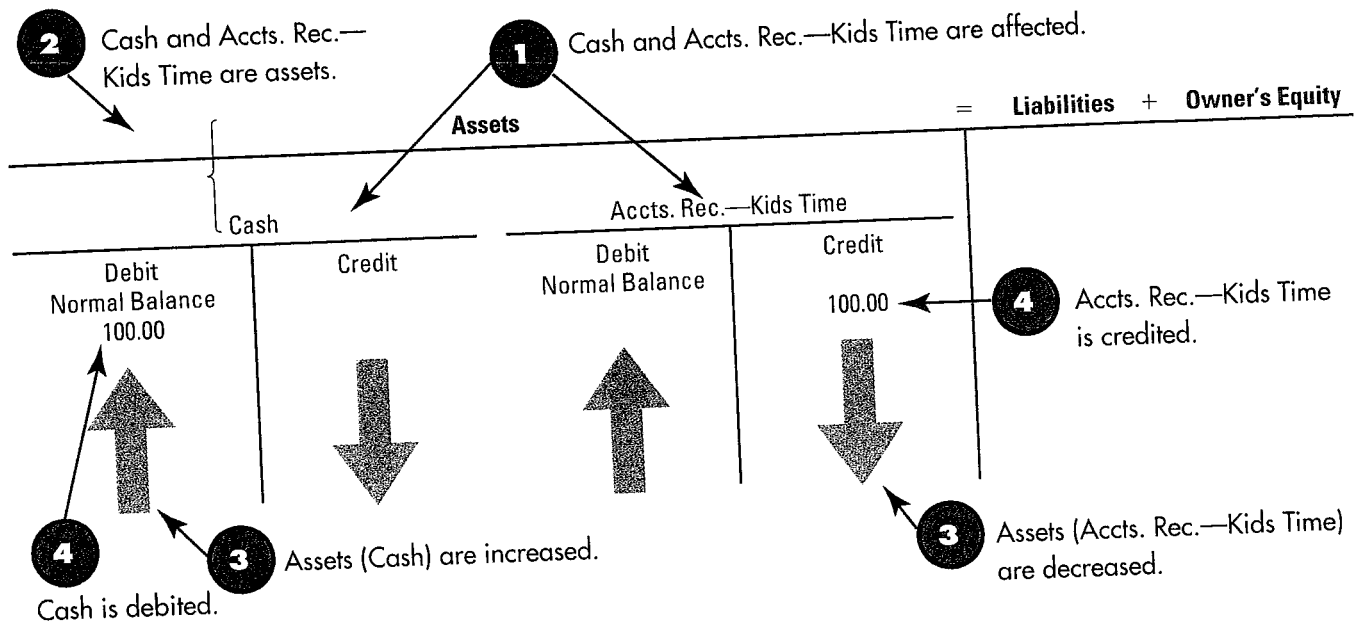
The owner's capital account has a normal credit balance. Decreases in the owner's capital account are shown as debits. Therefore, an expense account has a normal debit balance. Because expenses decrease owner's equity, increases in expenses are recorded as debits.

All expense transactions are recorded in a similar manner.

Questions for analyzing a transaction into its debit and credit parts

- Which accounts are affected?
Rent Expense and Cash
- How is each account classified?
Rent Expense is an expense account that affects owner's equity. Cash is an asset account.
- How is each classification changed?
Owner's equity is decreased by an increase in expenses. Assets are decreased.
- How is each amount entered in the accounts?
Owner's equity accounts decrease on the debit side. An increase in expenses decreases owner's equity. Expense accounts have normal debit balances. Therefore, the expense account, Rent Expense, is debited. Assets decrease on the credit side. Therefore, the asset account, Cash, is credited.

RECEIVED CASH ON ACCOUNT



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

S Questions for analyzing a transaction into its debit and credit parts

- T**
- E**
- P**
- S**
- Which accounts are affected?
Cash and Accounts Receivable—Kids Time
 - How is each account classified?
Cash is an asset account. Accounts Receivable—Kids Time is an asset account.
 - How is each classification changed?
Assets (Cash) are increased and assets (Accounts Receivable—Kids Time) are decreased.
 - How is each amount entered in the accounts?
Assets increase on the debit side. Therefore, the asset account, Cash, is debited. Assets decrease on the credit side. Therefore, the asset account, Accounts Receivable—Kids Time, is credited.



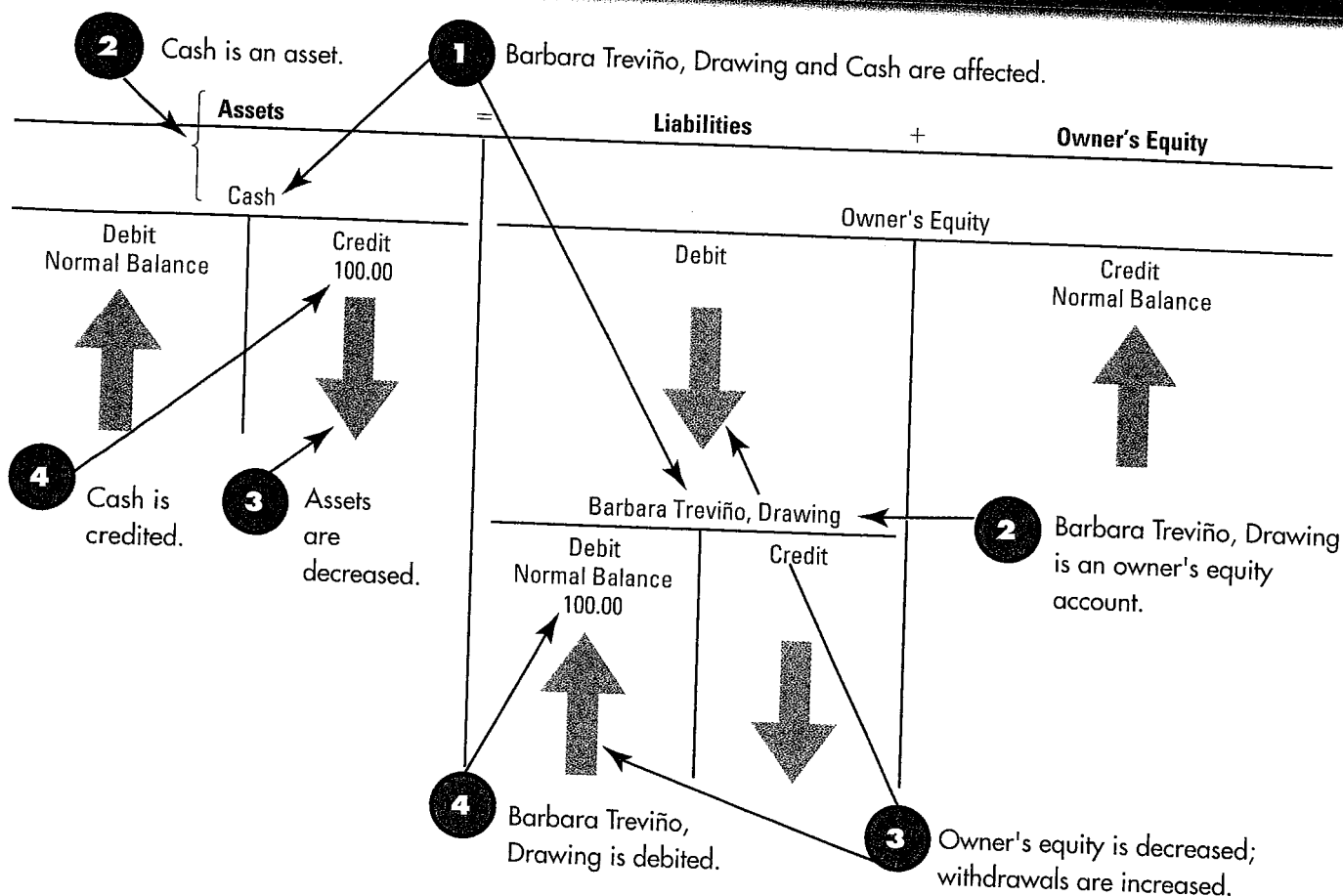
CULTURAL DIVERSITY

ANCIENT CHINA

By approximately 1000 B.C. the Chinese had developed one of the most sophisticated accounting systems in the world. The Chao Dynasty ruled China from 1122 to 256 B.C. During this time the dynasty oversaw territorial expansion and a Golden Age in literature and philosophy. The famous philosopher Confucius lived during this dynasty. Confucius was said to have been a government recordkeeper.

During the Chao Dynasty, the Chinese used a system of currency and had a central bank. The Office of the Superintendent of Records furnished compilations of receipts and payments. It also kept maps and records of production tools used. Many of the accounting and record keeping tasks that affect businesses and governments today can be traced back to systems established in ancient China.

PAID CASH TO OWNER FOR PERSONAL USE



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

Withdrawals decrease owner's equity. Withdrawals could be recorded directly in the owner's capital account. However, to avoid a

capital account with a large number of entries and to summarize withdrawal information separately from the other records, Encore Music uses a separate withdrawal account titled Barbara Treviño, Drawing.

STEPS Questions for analyzing a transaction into its debit and credit parts

- Which accounts are affected?
Barbara Treviño, Drawing, and Cash
- How is each account classified?
Barbara Treviño, Drawing is an owner's equity account. Cash is an asset account.
- How is each classification changed?
Owner's equity is decreased by an increase in withdrawals. Assets are decreased.
- How is each amount entered in the accounts?
Owner's equity accounts decrease on the debit side. An increase in withdrawals decreases owner's equity. Withdrawal accounts have normal debit balances. Therefore, the owner's equity account, Barbara Treviño, Drawing, is debited. Assets decrease on the credit side. Therefore, the asset account, Cash, is credited.

F.Y.I.

When drawing T accounts, stack the accounts instead of writing them horizontally. Stacking the accounts will make it easier to recognize debits and credits.

AUDIT YOUR UNDERSTANDING

1. What two accounts are affected when a business receives cash from sales?
2. What two accounts are affected when services are sold on account?
3. What two accounts are affected when a business pays cash to the owner for personal use?
4. Are revenue accounts increased on the debit side or credit side?
5. Are expense accounts increased on the debit side or credit side?

WORK TOGETHER

Analyzing revenue, expense, and withdrawal transactions into debit and credit parts

T accounts are given in the *Working Papers*. Your instructor will guide you through the following examples.

Use the chart of accounts for Bergum Services on page 50.

Transactions: Apr. 10. Received cash from sales, \$600.00.
11. Sold services on account to Sam Erickson, \$850.00.
14. Paid cash for rent, \$250.00.
18. Received cash on account from Sam Erickson, \$425.00.
20. Paid cash to owner for personal use, \$300.00.

6. Prepare two T accounts for each transaction. On each T account, write the account title of one of the accounts affected by the transaction.
7. Write the debit or credit amount in each T account to show the transaction's effect.

ON YOUR OWN

Analyzing revenue, expense, and withdrawal transactions into debit and credit parts

T accounts are given in the *Working Papers*. Work these problems independently.

Use the chart of accounts for Jens Accounting Service on page 50.

Transactions: Sept. 13. Received cash from sales, \$1,000.00.
15. Sold services on account to King Company, \$1,500.00.
16. Paid cash for utilities, \$500.00.
18. Received cash on account from King Company, \$750.00.
21. Paid cash to owner for personal use, \$650.00.

8. Prepare two T accounts for each transaction. On each T account, write the account title of one of the accounts affected by the transaction.
9. Write the debit or credit amount in each T account to show the transaction's effect.

After completing this chapter, you can

1. Define important accounting terms related to analyzing transactions into debit and credit parts.
2. Identify accounting practices related to analyzing transactions into debit and credit parts.
3. Use T accounts to analyze transactions showing which accounts are debited or credited for each transaction.
4. Analyze how transactions to set up a business affect accounts.
5. Analyze how transactions affect owner's equity accounts.

EXPLORE ACCOUNTING

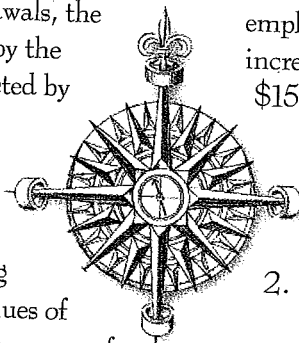
OWNER WITHDRAWALS

Employee salaries are considered an expense that reduces the net income of a company. When the owner withdraws cash from the company, this withdrawal is *not* considered an expense. The income of a business is calculated by subtracting total expenses from total revenue. Since withdrawals are not considered to be an expense, they do not affect the business's income.

A business owned by one person is called a proprietorship. The Internal Revenue Service does not require the proprietorship, itself, to pay taxes. However, the owner of the proprietorship must include the net income of

the proprietorship in his or her own taxable income.

Because the net income of a proprietorship is not affected by owner withdrawals, the income tax paid by the owner is not affected by how much cash the owner withdraws from the business. If Wang Accounting Services has revenues of \$2,500.00 and expenses of \$1,100.00, its net income is \$1,400.00 (\$2,500.00 - \$1,100.00). Wang Accounting Services will have net income of \$1,100.00 regardless of whether the owner withdraws \$100.00 or \$1,000.00 from the business during that period.



Discussion:

1. Ed Westing owns ESW Party Service. He is considering giving his employees a raise that would increase salaries by \$15,000.00 per year. What effect would this raise have on Mr. Westing's income tax?
2. Mr. Westing is also considering withdrawing \$5,000.00 from ESW Party Service for his personal use. What effect would this withdrawal have on the income tax Mr. Westing must pay this year?

3-1

APPLICATION PROBLEM

Determining the normal balance, increase, and decrease sides for accounts

Write the answers for the following problem in the *Working Papers*.

Cash
Accounts Receivable—Laurie Menz
Supplies
Prepaid Insurance

Accounts Payable—Gerald B's
Accounts Payable—VanDyke Company
Vivian Marx, Capital

1	2	3	4	5	6	7	8
Account	Account Classification	Account's Normal Balance		Increase Side		Decrease Side	
		Debit	Credit	Debit	Credit	Debit	Credit
Cash	Asset	✓		✓			✓

Instructions:

Do the following for each account. The cash account is given as an example.

- Write the account title in Column 1.
- Write the account classification in Column 2.
- Place a check mark in either Column 3 or 4 to indicate the normal balance of the account.
- Place a check mark in either Column 5 or 6 to indicate the increase side of the account.
- Place a check mark in either Column 7 or 8 to indicate the decrease side of the account.

3-2

APPLICATION PROBLEM

Analyzing transactions into debit and credit parts

John Burke owns John's Marketing Services, which uses the following accounts:

Cash
Supplies
Prepaid Insurance
Accounts Receivable—Orv Grant
Accounts Payable—D & S Company

John Burke, Capital
John Burke, Drawing
Sales
Advertising Expense
Rent Expense

Transactions:

- Mar. 1. Received cash from owner as an investment, \$1,500.00.
- Paid cash for insurance, \$600.00.
 - Bought supplies on account from D & S Company, \$800.00.
 - Paid cash for supplies, \$200.00.
 - Paid cash on account to D & S Company, \$400.00.

Instructions:

- Prepare two T accounts for each transaction. On each T account, write the account title of one of the accounts affected by the transaction. Use the forms in your *Working Papers*.

2. Write the debit or credit amount in each T account to show how the transaction affected that account. T accounts for the first transaction are given as an example.

MARCH 1.	Cash	
	1,500.00	
	John Burke, Capital	
		1,500.00

3-3

APPLICATION PROBLEM

Analyzing revenue, expense, and withdrawal transactions into debit and credit parts

Use the chart of accounts for John's Marketing Services given in Application Problem 3-2.

Transactions:

- Mar. 11. Received cash from sales, \$2,200.00.
 12. Paid cash for advertising, \$150.00.
 14. Sold services on account to Orv Grant, \$1,700.00.
 18. Paid cash to owner for personal use, \$500.00.
 19. Received cash on account from Orv Grant, \$1,000.00.

Instructions:

1. Prepare two T accounts for each transaction. On each T account, write the account title of one of the accounts affected by the transaction. Use the forms in your *Working Papers*.
2. Write the debit or credit amount in each T account to show how the transaction affected that account.

3-4

APPLICATION PROBLEM

Analyzing revenue, expense, and withdrawal transactions into debit and credit parts

Use the chart of accounts for John's Marketing Services given in Application Problem 3-2.

Transactions:

- Mar. 25. Sold services for cash, \$900.00.
 26. Performed \$750.00 of services for Orv Grant on account.
 27. Ran an ad in the local newspaper. Paid \$25.00 cash.
 28. John Burke withdrew \$450.00 for his personal use.
 29. Received a \$375.00 check from Orv Grant on account.

Instructions:

1. Prepare two T accounts for each transaction. On each T account, write the account title of one of the accounts affected by the transaction. Use the forms in your *Working Papers*.
2. Write the debit or credit amount in each T account to show how the transaction affected that account.

3-5

MASTERY PROBLEM

Analyzing transactions into debit and credit parts

Mark Lands owns a business called LandScape. LandScape uses the following accounts.

Cash	Mark Lands, Drawing
Accounts Receivable—Joseph Corbett	Sales
Accounts Receivable—Vera Rice	Advertising Expense
Supplies	Miscellaneous Expense
Prepaid Insurance	Rent Expense
Accounts Payable—Derner Office Supplies	Repair Expense
Accounts Payable—Janitor Supplies	Utilities Expense
Mark Lands, Capital	

Instructions:

1. Prepare a T account for each account. Use the forms in your *Working Papers*.
2. Analyze each transaction into its debit and credit parts. Write the debit and credit amounts in the proper T accounts to show how each transaction changes account balances. Write the date of the transaction in parentheses before each amount.

Transactions:

- June
1. Received cash from owner as an investment, \$3,000.00.
 2. Paid cash for supplies, \$60.00.
 4. Paid cash for rent, \$200.00.
 4. Received cash from sales, \$350.00.
 5. Paid cash for repairs, \$10.00.
 8. Sold services on account to Joseph Corbett, \$200.00.
 9. Bought supplies on account from Janitor Supplies, \$500.00.
 10. Paid cash for insurance, \$100.00.
 11. Received cash from owner as an investment, \$900.00.
 11. Received cash from sales, \$300.00.
 12. Bought supplies on account from Derner Office Supplies, \$50.00.
 13. Received cash on account from Joseph Corbett, \$125.00.
 15. Paid cash for miscellaneous expense, \$5.00.
 16. Paid cash on account to Janitor Supplies, \$50.00.
 22. Paid cash for electric bill (utilities expense), \$35.00.
 23. Paid cash for advertising, \$30.00.
 25. Sold services on account to Vera Rice, \$220.00.
 26. Paid cash to owner for personal use, \$600.00.
 30. Received cash on account from Vera Rice, \$100.00.

36

CHALLENGE PROBLEM

Analyzing transactions recorded in T accounts

Carol Burns owns a business for which the following T accounts show the current financial situation. Write the answers for the following problem in the *Working Papers*.

Cash			
(1)	5,000.00	(2)	80.00
(6)	475.00	(4)	15.00
(8)	350.00	(5)	16.00
(9)	400.00	(7)	900.00
		(10)	150.00
		(11)	95.00
		(12)	50.00

Accts. Rec.—David Gotch	
(13)	225.00

Supplies	
(3)	300.00
(11)	95.00

Accts. Pay.—Midwest Supplies	
(10)	150.00
(3)	300.00

Carol Burns, Capital	
(1)	5,000.00

Carol Burns, Drawing	
(2)	80.00

Sales	
(6)	475.00
(8)	350.00
(9)	400.00
(13)	225.00

Advertising Expense	
(5)	16.00

Miscellaneous Expense	
(4)	15.00

Rent Expense	
(7)	900.00

Utilities Expense	
(12)	50.00

1	2	3	4	5	6
Trans. No.	Accounts Affected	Account Classification	Entered in Account as a		Description of Transaction
			Debit	Credit	
1.	Cash Carol Burns, Capital	Asset Owner's Equity	✓	✓	Received cash from owner as an investment

Instructions:

- Analyze each numbered transaction in the T accounts. Write the titles of accounts affected in Column 2. For each account, write the classification of the account in Column 3.
- For each account, place a check mark in either Column 4 or 5 to indicate if the account is affected by a debit or a credit.
- For each transaction, write a brief statement in Column 6 describing the transaction. Information for Transaction 1 is given as an example.