**The Recording Process**

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## The Father of Accounting

**Luca Pacioli** was known as the **Father of Accounting**. He was an Italian Mathematician and a Franciscan Friar. In 1494, he wrote a book called Summa de Arithmetica, Geometrica, Proportioni er Proportionalitia, in which he introduced the **double-entry system** used throughout accounting.

## Double-Entry System

The **double-entry system** states that each transaction must affect two or more accounts, in order to keep the basic accounting equation in balance. In other words, for each transaction, debits (Dr.) must equate credits (Cr.) in accounts.

The table below summarizes how each account type is affected by debits and credits:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Normal Balance | On Increase | On Decrease |
| Assets | Debit | Debit | Credit |
| Liabilities | Credit | Credit | Debit |
| Owner’s Capital | Credit | Credit | Debit |
| Revenues | Credit | Credit | Debit |
| Expenses | Debit | Debit | Credit |
| Drawings | Debit | Debit | Credit |

In the table above, revenues and expenses only ever decrease when a company makes an error (increased the value too much in the previous month) that they need to correct.

## Journals

A journal records transactions. An example of a journal is provided below:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Campus Laundromat | | | | | | |
| Journal | | | | | | |
| Date | Accounts Title | | | Ref. | Debit ($) | Credit ($) |
| 2019 |  |  |  |  |  |  |
| Jan 01 | Cash | | Dr. |  | 500 |  |
|  |  | Service Revenue | Cr. |  |  | 500 |
| Jan 03 | Rent Expense | | Dr. |  | 300 |  |
|  |  | Cash | Cr. |  |  | 300 |
| Jan 05 | Equipment | | Dr. |  | 10,000 |  |
|  |  | Cash | Cr. |  |  | 6,000 |
|  |  | Accounts Payable | Cr. |  |  | 4,000 |
| Jan 07 | Cash |  | Dr. |  | 10,000 |  |
|  |  | Owner’s Capital | Cr. |  |  | 10,000 |
| Jan 08 | Accounts Payable | | Dr. |  | 4,000 |  |
|  |  | Cash | Cr. |  |  | 4,000 |
| Jan 10 | Accounts Receivable | | Dr. |  | 5,000 |  |
|  |  | Service Revenue | Cr. |  |  | 5,000 |
| Jan 13 | Cash | | Dr. |  | 500 |  |
|  |  | Accounts Receivable | Cr. |  |  | 500 |

In the table above, we have two types of entries. Entries that affect two accounts are called **simple entries**. Entries that affect more accounts are called **compound entries**.

The **account titles** used in the journal must exactly match those provided in the **Chart of Accounts**, which is just a list of account titles.

The **reference column** can be left empty.

## Unearned Revenues and Prepaid Expenses

There are two types of transactions that we have not yet explored, unearned revenues and prepaid expenses.

Suppose a customer gives us an advance on a job that we have not yet performed. Such a transaction is called an **Unearned Revenue**. It is a **current liability**.

|  |  |  |
| --- | --- | --- |
| Cash | | Dr. |
|  | Unearned Revenue | Cr. |

Once the service is actually provided, we have a corresponding transaction to get rid of the liability.

|  |  |  |
| --- | --- | --- |
| Unearned Revenue | | Dr. |
|  | Service Revenue | Cr. |

Similarly, if we make an advance payment on something, such as insurance, it is called a **prepaid expense**. Prepaid expenses are **current assets**.

|  |  |  |
| --- | --- | --- |
| Prepaid Insurance | | Dr. |
|  | Cash | Cr. |

Once the expense is actually incurred, we lose the asset. In the case of insurance, this occurs part by part on a monthly basis.

|  |  |  |
| --- | --- | --- |
| Insurance Expense | | Dr. |
|  | Prepaid Insurance | Cr. |

## Ledgers

A **Ledger** is a classification of all the transactions occurring in each account.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Campus Laundromat | | | | | |
| General Ledger | | | | | |
|  | | | | | |
| Cash | | | | | |
| Date | Explanation | Ref. | Debit ($) | Credit ($) | Balance ($) |
| 2010 |  |  |  |  |  |
| Sept. 1 |  |  | 20,000 |  | 20,000 |
| Sept. 2 |  |  |  | 1,000 | 19,000 |
| Sept. 3 |  |  |  | 10,000 | 9,000 |
| Sept. 4 |  |  |  | 1,200 | 7,800 |
| Sept. 20 |  |  |  | 700 | 7,100 |
| Sept. 30 |  |  | 6,200 |  | 13,300 |
|  | | | | | |
| Bob Sample, Capital | | | | | |
| Date | Explanation | Ref. | Debit ($) | Credit ($) | Balance ($) |
| 2010 |  |  |  |  |  |
| Sept. 1 |  |  |  | 20,000 | 20,000 |

The **reference** and **explanation** columns can be left empty. Every account must be included in the ledger, even though just two are shown.

## Trial Balance

A **trial balance** is a summary of the accounts.

|  |  |  |
| --- | --- | --- |
| Pioneer Advertising Agency | | |
| Trial Balance | | |
| October 31, 2010 | | |
| Account Title | Debit ($) | Credit ($) |
| Cash | 15,200 |  |
| Advertising Supplies | 2,500 |  |
| Prepaid Insurance | 600 |  |
| Office Equipment | 5,000 |  |
| Notes Payable |  | 5,000 |
| Accounts Payable |  | 2,500 |
| Unearned Revenue |  | 1,200 |
| C.R. Byrd, Capital |  | 10,000 |
| C.R. Byrd, Drawings | 500 |  |
| Service Revenue |  | 10,000 |
| Salaries Expense | 4,000 |  |
| Rent Expense | 900 |  |
|  | 28,700 | 28,700 |