



The Simple Ledger DR/CR Rules

Chapter 4





AGENDA

- ▶ Source documents
- ▶ GAAP – objectivity principle
- ▶ Ledger accounts
- ▶ Important features of ledger accounts
- ▶ DR/CR Rules
- ▶ Calculating the balances of accounts
- ▶ Buying & selling on credit / account
- ▶ The trial balance
- ▶ How to create a trial balance
- ▶ Importance of trial balance




Source Documents






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ITEMS SOLD 3




Invoice #1000
Oct 1, 2008



Source Documents


- ▶ Source documents are the original business papers such as receipts, invoices, cheques, bank statements, credit card statements.
- ▶ They provide proof of payment, proof of purchase, and reference.

1. Accounting entries are made from source documents
2. Source documents are stored for reference and as proof




GAAP – Objectivity Principle

- ▶ Objectivity Principle:
 - ▶ accounting records should be based on the objective evidence provided by source documents to support their values.
- ▶ Amounts are determined using source documents and not on personal opinions.



Ledger Accounts

- ▶ An account is a record that documents each change to items in the accounting equation.
- ▶ There is one account for each asset, each liability, and each type of equity.
- ▶ A **ledger** is a *group of accounts*.
- ▶ Ledger accounts are often referred to as T-accounts.



Ledger Accounts



Assets			Liabilities + Owner's Equity		
Cash	A/R W. Caruso	A/R R. Van Loon	Bank Loan	A/P Dini Bros.	A/P Packham Products
3 285	150	620	18 000	1 516	3 946
Supplies	Trucks	Equipment	B. Ristien, Capital		
2 465	55 075	22 174	60 287		

Important Features of Ledger Accounts

- ▶ Each individual balance sheet item is given its own T-account with the name of the item at the top.
- ▶ The dollar figure for each item is recorded in the account on the first line. This is the beginning value for the account.



Important Features of Ledger Accounts

- ▶ For any item, the correct side for its beginning value is the side on which the item itself would appear in the accounting equation $A = L + OE$.
- ▶ For assets, the beginning values are on the left side
- ▶ For liabilities and owner's equity, they are on the right side



DR/CR Rules



Assets		=	Liabilities		+	Owner's Equity	
DR	CR		DR	CR		DR	CR
+	-		-	+		-	+
↑	↓		↓	↑		↓	↑

DR/CR Rules

- ▶ Remember:
 - ▶ DR means the left side of the account
 - ▶ CR means the right side of the account



- ▶ For each type of account, its record increases from its beginning value side and decreases on the other side
 - ▶ For assets, DR increases, CR decreases
 - ▶ For liabilities, DR decreases, CR increases
 - ▶ For owner's equity, DR decreases, CR increases



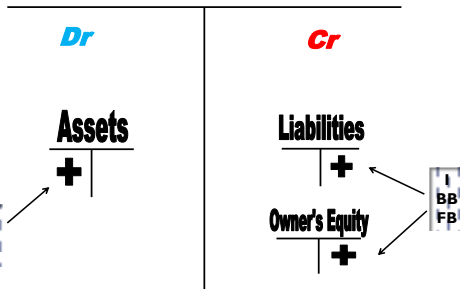
DR/CR Rules

- ▶ This is called the double entry system
- ▶ Double entry means that you do 2 entries for each transactions (shock!) – in separate accounts
- ▶ Notice that each transaction has a DR and a CR amount
- ▶ **DEBITS must equal CREDITS for each transaction**
- ▶ Each transaction will result in a change to at least two accounts.
- ▶ The accounts may increase or decrease.
- ▶ Do NOT think in terms of a DR being an increase or a CR being a decrease.




▶ <http://www.newlearner.com/courses/hts/baf3m/bac105.htm>

T-Account



I-increase; *BB*-beginning balance; *FB*-final balance

Calculating the **Balances** of Accounts

- ▶ The **account balance** gives the dollar value of an account and shows whether it is a DR or Cr value.
 - ▶ DR and CR have opposite effects on accounts
 - ▶ To calculate balances:
 - ▶ Add the 2 sides of the account separately
 - ▶ Take the larger total and subtract the smaller total from it
 - ▶ Write the result on the side of the larger total
- 



Calculating the Balances of Accounts

ASSETS			LIABILITIES + EQUITY		
Bank	A/R W. Curcio	A/R R. Van Loon	Bank Loan	A/P Doe Bros.	A/P Packham Products
1 365 ② 200 ③ 450 4 665 5 665 ⑥ 215	150 3 900 4 050	⑤ 420 350 770 100	18 000	④ 500 1 515 5 500 7 015 6 515	3 945 200 4 145
Supplies	Trucks	Equipment	B. Rosen, Capital		
2 465 ① 200 3 665 ④ 675	53 075 ③ 8 000 61 075	22 174	60 187 ⑦ 400 350 ⑧ 67 61 044		



Buying & Selling on Account

- ▶ The term **“on account”** is used extensively in business in 4 ways:
- ▶ If you **purchase** an item and would like to pay **later**, this is a **purchase on account**.
 - ▶ If you **sell** an item and your customer will pay you **later**, this is a **sale on account**.
 - ▶ When you pay the money that you owed earlier, it is a **payment on account**.
 - ▶ When you receive money that your customer owed you, it is a **receipt/received on account**.



The Trial Balance

PIONEER ADVERTISING AGENCY		
Trial Balance		
October 31, 2002		
	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. Drawings	500	
Service Revenue		10,000
Salaries Expense	4,000	
Rent Expense	900	
	28,700	28,700

The total credits MUST equal the total debits



How to create a Trial Balance

- A T/B is a list of accounts and their balances at a given time.
- The primary purpose of a T/B is to prove the mathematical equality of DR and CR.
- A T/B also uncovers errors.

- The procedures for preparing a T/B are:
 - Write the 3-line heading at the top
 - List the account titles and their balances
 - Total the DR and CR columns
 - Ensure the totals of the 2 columns are the same
 - If yes = "**in balance**"
 - If not = "**out of balance**"



Importance of a Trial Balance

- ▶ It is essential to have the ledger in balance with the accounting equation
- ▶ An out of balance ledger is a sign that an error has been made
- ▶ All errors must be found and corrected

