ΟΙΚΟΝΟΜΙΚΟ ΠΑΝΕΠΙΣΤΗΜΙΟ ΑΘΗΝΩΝ
ATHENS UNIVERSITY OF ECONOMICS AND BUSINESS

Financial and Management Accounting
Journal Entries

Leonidas Doukakis
Professor

MSc in International Shipping, Finance and Management

Objectives

After this session, participants are expected to:

- ✓ Be able to analyze transactions
- ✓ Understand how accounting works
- ✓ Be able to record transactions in the journal (double-entry bookkeeping)
- ✓ Be able to prepare a trial and an adjusted trial balance
- ✓ Be able to analyze transactions using T-accounts
- ✓ Be able to understand the differences between cash profit and accounting profit
- ✓ Be able to record adjusting entries

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Double-Entry Accounting

Recording in a Journal

Trial and Adjusted Trial Balance

Accrual Accounting Vs. Cash Accounting

- Prepaid Expenses
- Accrued Expenses
- Accrued Revenues
- Unearned Revenues

ACCOUNTING BASICS ENTRIES

Double-Entry Accounting

- All business transactions include two parts:
  - You give something.
  - You receive something.

→ Double-entry system

- Each transaction affects at least two accounts (two-sided effect).

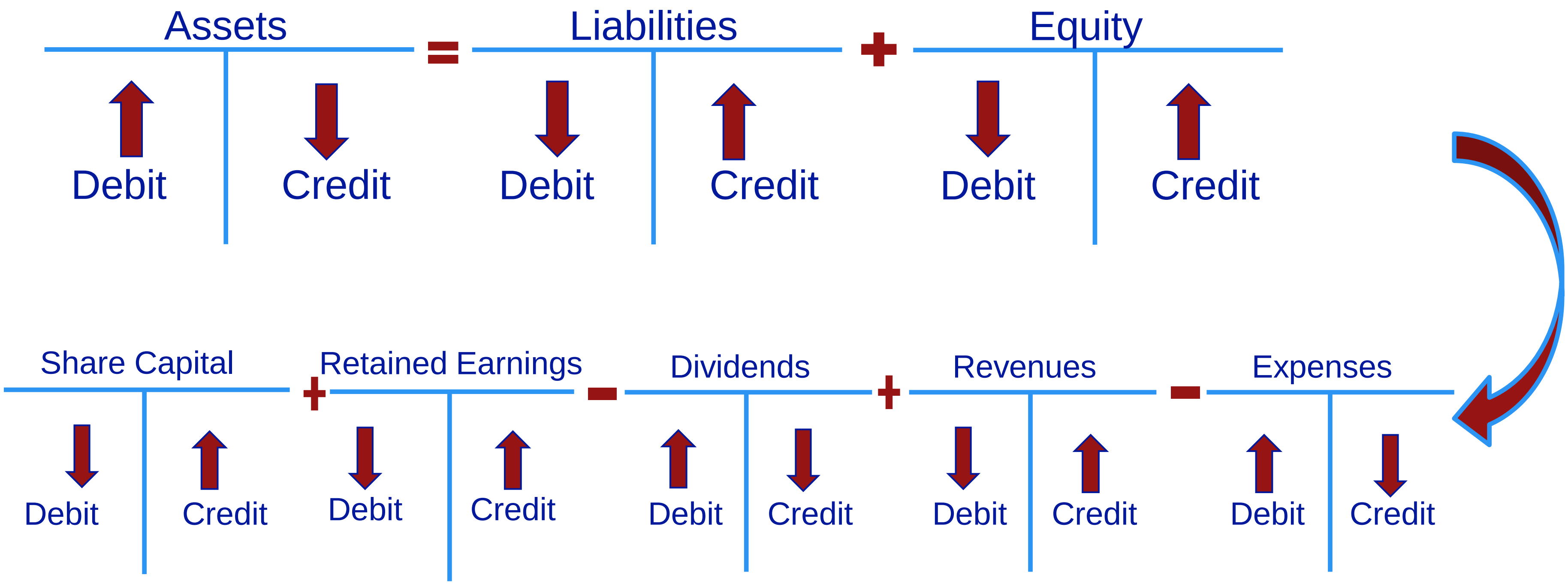
- An account can be represented by the letter T (T-account).

Account name	
Debit	Credit

- Every business transaction involves both a debit and a credit. The total debits and credits for every business transaction <u>must be equal</u>.

Debit & Credit Rules

- The type of account determines how we record increases and decreases.



T-Accounts

- The balance in an account is the difference between the sum of the debits and the sum of the credits.

Cash

Beg. Bal. 1,100	250
200	120
340	80
End. Bal.1,190	

Accounts Payable

800	1,250 Beg. Bal.
200	200
	180
	630 End. Bal.

- Accounts that are increased with debits, have normal debit balances.
  - Assets, Dividends, Expenses.

- Accounts that are increased with credits, have normal credit balances.
  - Liabilities, Share Capital, Retained Earnings, Revenues.

Accrual VS Cash-Basis Accounting

- **Accrual accounting** records the impact of transactions when they occur and **not** when the money is received or paid.
  - Revenues are recognized when earned.
  - Expenses are recognized when incurred.

Examples of cash transactions: Sales in cash, receiving cash from interest earned, paying salaries and other expenses, paying of loans etc.

Examples of non-cash transactions: Purchases of inventory on account, depreciation expense, usage of prepaid rent and insurance, earning of revenue when cash was collected in advance etc.

- **Cash-Basis accounting** records only cash transactions (cash receipts and payments).
  - Revenues are recognized when cash is received.
  - Expenses are recognized when cash is paid.

Recording in a Journal – Posting to the Ledger

Accounting transactions are recorded

in a chronological order in the **journal**.

General Journal					
Date		Account Title and Explanation	Post Ref	Debit	Credit
2014					
April	1	Cash		10,000.00	
		Common Stock			10,000.00
		To record the issuance of 10,000 shares of common stock at par value to Andrea Seffler to start the company.			
	2	Office Supplies		225.00	
		Cash			225.00
		To record the purchase of office supplies for cash.			

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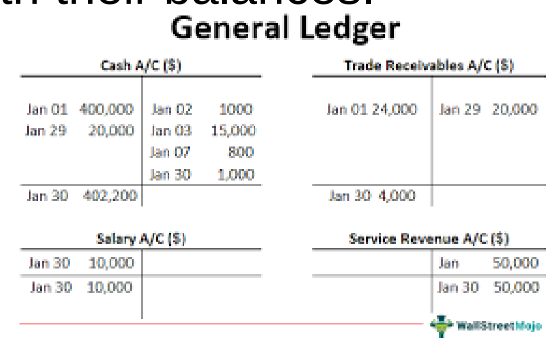
Steps:

1. Specify each account affected by the transaction.
2. Classify each account either as asset, liability, equity, revenue, or expense.
3. Determine whether the account is increased or decreased and then use the rules of debit and credit.
4. Record the transaction in the journal including a brief explanation.

- The **ledger** is a grouping of all the T-accounts, with their balances.
- **Posting** is the process of transferring debits

and credits from journal to ledger.



The Trial Balance

- A **trial balance** lists all open accounts with their balances.
- Assets first, then liabilities and stockholders' equity.
- The trial balance:
  - ✓ Summarizes account balances.
  - ✓ Shows whether total debits equal total credits.

Trial Balance
December 31, 2005

Account Title	Debit	Credit
Cash	$7,000	
Accounts Receivable	3,000	
Office Supplies	3,000	
Office Equipment	5,000	
Bank Loan		$5,000
Accounts Payable		1,000
Common Stock		10,000
Consulting Revenue		7,000
Rent Expense	600	
Salaries Expense	2,500	
Supplies Used	1,200	
Utilities Expense	700	
Total	$23,000	$23,000

Small Case: *ALK SERVICES*

20 min

Revenue Recognition & Matching Principle

- Revenue is recognized when :

  1. It is **earned** (i.e., performance obligation is satisfied); and

  2. Cash collection is **reasonably assured**

- For sales, a useful question to ask is:

  have the ‘**risks and rewards**’ of ownership been transferred?

- The **matching principle** is the basis for recording and recognizing expenses. Revenues earned are matched with expenses incurred in earning those revenues. (e.x. Sales and C.G.S.)

- Expenses can be deferred until revenues are recognized **only if** they satisfy asset definition.

Expenses Matching: Timing

- Assets provide future benefits to the firm and are consumed in the process of generating revenues
- As assets are consumed, the value of the remaining asset is reduced and an expense is incurred (e.g. depreciation, supplies used, COGS)
- Expenses are “expired costs” or “gone assets”

Asset: Economic resource controlled by a company that is used to produce revenue and that is expected to provide future economic benefits

Liability: Present obligation of a business to relinquish assets, provide services, or accept other obligations

Expense: An economic sacrifice (a decrease in assets or an increase in liabilities) resulting from operating activities undertaken to generate revenues

Revenue: An economic benefit (an increase in assets or a decrease in liabilities) gained by providing goods or services to customers

Accrual Accounting

Prepaid Expenses: Expenses paid in cash before they are used or consumed

Assets

Accrued Expenses: Expenses incurred, but not yet paid or recorded.

Liabilities

Accrued Revenues: Revenues earned, but cash not yet received.

Assets

Unearned Revenues: Cash received before services are performed.

Liabilities

Prepaid Expenses

Prepaid Expenses provide future economic benefits.

Prepaid expenses should be adjusted, before the preparation of the financial statements, in order to:

- Reflect the amount of expenses incurred in the current period ⟹ Expense recognition
- Reflect the amount of prepaid expenses that will be incurred in the future periods

Example: The company prepaid the insurance 12,000 for the next 12 months on October 1st, 2022.

Oct. 1, 2022	Prepaid Insurance	12,000	
	Cash		12,000
	Payment of 12 months insurance in advance		
Dec. 31, 2022	Insurance Expense	3,000	
	Prepaid Insurance		3,000
	Expense 3 months insurance		

Prepaid Insurance

12,000	3,000
Balance Sheet 9,000	

Insurance Expense

3,000	
Income Statement 3,000	

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Accrued Expenses

Accrued Expenses reflect liabilities arising from an expense that has not yet been paid.

Accrued Expenses should be adjusted, before the preparation of the financial statements, in order to:

- Reflect the amount of expenses incurred in the current period ⟹ Expense adjustment
- Reflect the amount of accrued expenses that will be settled in future periods

<u>Example</u>: The company pays its employees a monthly salary of 3,600, half on the 15th and half on the last day of the month. Apr. 30, 2022 is a Sunday. Payment will be made on the May., 1, 2022.

Apr. 15, 2022	Salary Expense	1,800	
	Cash		1,800
	Salary payment		
Apr. 30, 2022	Salary Expense	1,800	
	Salary Payable		1,800
	Accrued Salary Expense		

Salary Expense

Debit	Credit
1,800	
1,800	

Income Statement 3,600

Salary Payable

Debit	Credit
	1,800

Balance Sheet 1,800

Accrued Revenues

Accrued Revenues reflect revenues that have been earned but have not yet been collected.

Accrued Revenues should be adjusted, before the preparation of the financial statements, in order to:

- Reflect the amount of revenues earned in the current period ⟹ Revenue adjustment
- Reflect the amount of accrued revenues that will be collected in future periods

Example: The company provides services to a customer on a monthly basis (200 per month) beginning in Oct. 1, 2022. The customer will pay at the end of February 2023.

Dec. 31, 2022	Accounts Receivable	600	
	Service Revenue		600
	Service revenue		

Accounts Receivable

Debit	Credit
600	
Balance Sheet 600	

Service Revenue

Debit	Credit
	600
	Income Statement 600

Unearned Revenues

Unearned Revenues (Deferred Income) reflect a liability that arises from receiving cash before providing a service.

Unearned Revenues should be adjusted, before the preparation of the financial statements, in order to:

- Reflect the amount of revenues earned during the current period
- Reflect the amount of liabilities that will be settled in future periods by providing the relevant services

Example: The company enters into an agreement to continuously provide services to a customer for the next 3 years. The customer pre-pays the services (800) for the first 4 months (1/10/2022-31/1/2023).

Oct. 1, 2022	Cash	800	
	Unearned Service Revenue		800
	Received cash for revenue in advance		
Dec. 31, 2022	Unearned Service Revenue	600	
	Service Revenue		600
	Service revenue earned		

Unearned Ser. Rev.

600	800
	Balance Sheet 200

Service Revenue

	600
	Income Statement 600

The Adjusted Trial Balance and Closing Entries

- The previous four types of entries are called **Adjusting Entries**. Adjusting Entries are made at the end of an accounting period to bring all accounts up to date on an accrual basis, so that the company can prepare correct financial statements.

- An **Adjusted Trial Balance** lists all open accounts with their balances immediately after all **adjustments** have been posted.

- A trial balance taken immediately **after closing** entries have been posted is called **Post-Closing Trial Balance**.

- **Closing Entries**: the formal process by which companies reduce all account Income statement accounts to zero and determine and transfer the net income or net loss to an equity account.

Small Case: *SAFIRA Plc*

20 min

Small Case: *MIDA Plc*

20 min

QUESTIONS