

# CHAPTER 3

## The Accounting Information System

### ANSWERS TO QUESTIONS

1. The system of collecting and processing transaction data and communicating financial information to decision makers is known as the accounting information system.
2. Yes, a business can enter into a transaction in which only the left side of the accounting equation is affected. An example would be a transaction where an increase in one asset is offset by a decrease in another asset. An increase in the equipment account which is offset by a decrease in the cash account is a specific example.
3. Accounting transactions are the economic events of the company recorded by accountants because they affect the basic accounting equation.
  - (a) The death of a major stockholder of the company is not an accounting transaction as it does not affect the basic accounting equation.
  - (b) Supplies purchased on account is an accounting transaction because it affects the basic accounting equation.
  - (c) An employee being fired is not an accounting transaction as it does not affect the basic accounting equation.
  - (d) Paying a cash dividend to stockholders is an accounting transaction as it does affect the basic accounting equation.
4.
  - (a) Decrease assets and decrease stockholders' equity.
  - (b) Increase assets and decrease assets.
  - (c) Increase assets and increase stockholders' equity.
  - (d) Decrease assets and decrease liabilities.
5. An account consists of three parts: (a) the title, (b) the left or debit side, and (c) the right or credit side. Because the alignment of these parts resembles the letter T, it is referred to as a T account.
6. Disagree. The terms debit and credit are synonymous with left and right, respectively.
7. Terry is incorrect. The double-entry system merely records the dual (two-sided) effect of a transaction on the accounting equation. A transaction is not recorded twice; it is recorded once, and must affect two or more accounts to keep the basic accounting equation in balance. In other words, for each transaction, debits must equal credits.
8. Misty is incorrect. A debit balance only means that debit amounts exceed credit amounts in an account. Conversely, a credit balance only means that credit amounts are greater than debit amounts in an account. Thus, a debit or credit balance is neither favorable or unfavorable.
9.
  - (a) Asset accounts are increased by debits and decreased by credits.
  - (b) Liability accounts are decreased by debits and increased by credits.
  - (c) The common stock account is decreased by debits and increased by credits.

**Questions Chapter 3 (Continued)**

10. (a) Accounts Receivable—debit balance.  
 (b) Cash—debit balance.  
 (c) Dividends—debit balance.  
 (d) Accounts Payable—credit balance.  
 (e) Service Revenue—credit balance.  
 (f) Salaries and Wages Expense—debit balance.  
 (g) Common Stock—credit balance.
11. (a) Accounts Receivable—asset—debit balance.  
 (b) Accounts Payable—liability—credit balance.  
 (c) Equipment—asset—debit balance.  
 (d) Dividends—stockholders' equity—debit balance.  
 (e) Supplies—asset—debit balance.
12. (a) Debit Supplies and credit Accounts Payable.  
 (b) Debit Cash and credit Notes Payable.  
 (c) Debit Salaries and Wages Expense and credit Cash.
13. (a) Cash—both debit and credit entries.  
 (b) Accounts Receivable—both debit and credit entries.  
 (c) Dividends—debit entries only.  
 (d) Accounts Payable—both debit and credit entries.  
 (e) Salaries and Wages Expense—debit entries only.  
 (f) Service Revenue—credit entries only.
14. Normal balances for accounts in Tootsie Roll's financial statements: Accounts Receivable—debit; Income Taxes Payable—credit; Sales—credit; Selling, Marketing, and Administrative Expenses—debit.
15. The basic steps in the recording process are:  
 (1) Analyze each transaction in terms of its effect on the accounts.  
 (2) Enter the transaction information in a journal.  
 (3) Transfer the journal information to the appropriate accounts in the ledger.
16. (a) The debit should be entered first.  
 (b) The credit should be indented.
17. (a) No, debits and credits should not be recorded directly in the ledger.  
 (b) The advantages of using the journal are:  
 (1) It discloses in one place the complete effect of a transaction.  
 (2) It provides a chronological record of all transactions.  
 (3) It helps to prevent or locate errors because the debit and credit amounts for each entry can be readily compared.
18. (a) Cash ..... 12,000  
     Common Stock ..... 12,000  
     (Issued stock for cash)
- (b) Prepaid Insurance ..... 800  
     Cash ..... 800  
     (Paid one-year insurance policy)

**Questions Chapter 3 (Continued)**

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|-----|---------------------------------------|-------|-------|
| (c) | Supplies .....                        | 1,800 |       |
|     | Accounts Payable .....                |       | 1,800 |
|     | (Purchased supplies on account)       |       |       |
| (d) | Cash .....                            | 7,500 |       |
|     | Service Revenue .....                 |       | 7,500 |
|     | (Received cash for services rendered) |       |       |
- 19.** (a) The entire group of accounts maintained by a company, including all the asset, liability, and stockholders' equity accounts, is referred to collectively as the ledger.  
(b) The chart of accounts is important, particularly for a company that has a large number of accounts, because it helps organize the accounts and identify their location in the ledger.
- 20.** A trial balance is a list of accounts and their balances at a given time. The primary purpose of a trial balance is to prove the mathematical equality of debits and credits after all journalized transactions have been posted. A trial balance also facilitates the discovery of errors in journalizing and posting. In addition, it is useful in preparing financial statements.
- 21.** The proper sequence is as follows:  
(b) Accounting transaction occurs.  
(c) Information is entered in the journal.  
(a) Debits and credits are posted to the ledger.  
(e) Trial balance is prepared.  
(d) Financial statements are prepared.
- 22.** (a) The trial balance would balance.  
(b) The trial balance would not balance since the debits would be \$720 higher than the credits.