# Three Fundamental Bookkeeping Equations

**Assets = Liabilities + Stockholders' Equity** 

**Sum of Debits = Sum of Credits** 

Beginning account balance + Increases - Decreases = Ending account balance

- These equations must be in balance at all times!
- The balance sheet equation can be preserved through the use of "debits" and "credits"
- Definitions of Debit and Credit:
  - Debit (Dr.) = Left-side Entry
  - Credit (Cr.) = Right-side Entry



## **Debit/Credit Bookkeeping**

```
Assets = Liabilities + Shareholders' Equity

Assets = Liabilities + Contrib. Capital + Retained Earnings + Revenues - Expenses

Assets + Expenses = Liabilities + Contrib. Capital + Retained Earnings + Revenues

Debits = Credits
```

- Rules of Debits and Credits:
  - Every transaction must have at least one debit and at least one credit
  - Debits must equal credits for all transactions
  - No negative numbers are allowed



## **Accounts and Account Balances**

#### Normal Balance

 The type of balance (debit or credit) the account carries under normal circumstances

#### T Account

- A record of all changes in an accounting quantity
- Debits are listed on the left side of the T
- Credits are listed on the right side of the T

#### Account Balance

- Difference between sum of debits and sum of credits for the account
- Change in Account Balance Equation:
  - Beginning Balance + Increases Decreases = Ending Balance



## **Normal Balances and T-accounts**

## Assets, Expenses

- Normal Balance is Debit (Left side of T)
- Increases through Debits (Left entries)
- Decreases through Credits (Right entries)
- Beginning (Debit) Balance + Debits Credits = Ending (Debit) Balance

### Accounts Receivable (A)

Beg. Balance	1,000	
New Sales (Increase)	100	80 Cash Collections (Decrease)
End. Balance	1,020	



## **Normal Balances and T-accounts**

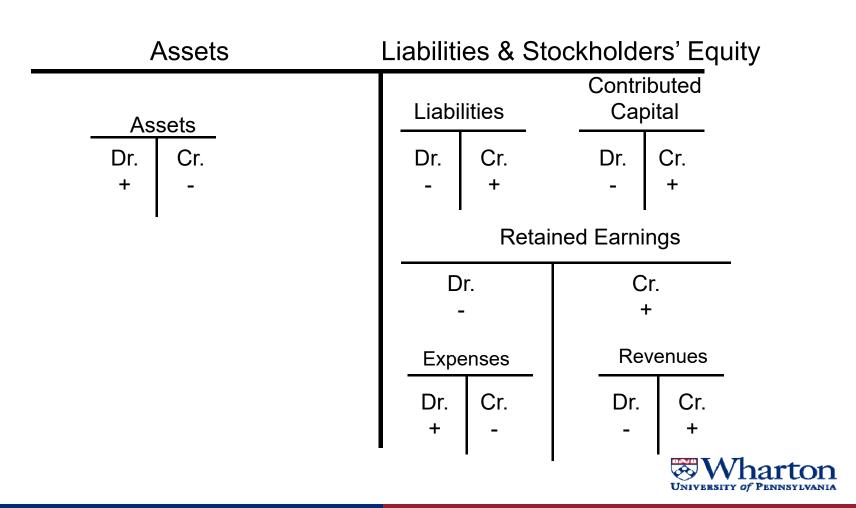
- Liabilities, Stockholders' Equity, Revenues
  - Normal Balance is Credit (Right side of T)
  - Decreases through Debits (Left entries)
  - Increases through Credits (Right entries)
  - Beginning (Credit) Balance + Credits Debits = Ending (Credit) Balance

### Accounts Payable (L)

		1,00	0	Beg. Balance
Cash Payments (Decrease) 80		100 New Purchases (Increase)		
		1,020	0	End. Balance



## **Super T-account**



# **Analyzing Transactions & Journal Entries**

- Three questions in analyzing transactions
  - Which specific asset, liability, stockholders' equity, revenue or expense accounts does the transaction affect?
  - Does the transaction increase or decrease the affected accounts?
  - Should the accounts be debited or credited?
- Journal entry format

Dr. <Name of Account Debited> \$XXX

Cr. <Name of Account Credited> \$XXX

Always list Debits first and always indent Credits

