DEFINITION of 'Accounting Principles'

The rules and guidelines that companies must follow when reporting financial data. The common set of [accounting](http://www.investopedia.com/terms/a/accounting.asp) principles is the [generally accepted accounting principles (GAAP).](http://www.investopedia.com/terms/g/gaap.asp) To remain listed on many major stock exchanges in the U.S., companies must file regular [financial statements](http://www.investopedia.com/terms/f/financial-statements.asp) reported according to GAAP. Accounting principles differ around the world, and countries usually have their own, slightly different, versions of GAAP

# Three Golden Rules of Accounting with Examples

Creating journal entries requires some rules, such rule is named as Three Golden Rules of Accounting standards. There are three kinds of account as Personal Account, Real Account and Nominal Account. Let’s see the rules for those different account from scratch and in detail.

## 1. Personal Account

Personal account relates to persons with whom a business keeps dealings. A person called be a natural person or a legal person. If a person receives anything from the business, he is called receiver and his account is to debited in the books of the business. If person gives anything to business, he is called as a giver and his account is to be credited in the books of the business.

The Golden Rule for Personal Account is,

**Debit the Receiver and Credit the Giver**

**Example:** Goods worth 1000 bucks sold to Mr. Smith from Mr. John. In this transaction, Mr. Smith is the receiver of goods, he is called receiver and his account is to be debited in the books of business. Mr. John is the giver of goods, he is called giver and his account is to be credited in the books of business.

## 2. Real Account

Real account relates to property which may either come into the business or go from business. If any property or goods comes into the business, account of that property or goods is to be debited in the books of the business. If any property or goods goes out from the business account of that property or goods is to be credited in the books of business.

The Golden Rule for Real Account is,

**Debit What Comes in and Credit What Goes out**

**Example:** Goods sold on cash for 1500 bucks. In this transaction cash, an assets for business comes into the business on sales of goods, and therefore cash account is to be debited in the books of business. On the other side, goods, an assets of business goes out of the business on sale and therefore goods account is to be credited in the books of business.

## 3. Nominal Account

Nominal account is an account that relates to business expenses, loss, income and gains. If business incurs expense to manage and run business, account of that expense is to be debited in the books of business. When a business earns income by rendering services or hiring business assets, an account of that income is to credited in the books of business.

On other hand, if in the case the transaction of sale or purchase of goods or assets, if any loss is incurred by the business, account of that loss is to debited in the books or assets. if in the transaction of sale or purchase of goods or assets any profit is earned by the business, then account of that profit is to be credited in the books of business.

The Golden Rule for Nominal Account is,

**Debit all Expenses or Loss and Credit all Income Gains or Profit**

**Example:** (1) Paid 50 bucks as a commission to our agent, here commission which is paid to an agent is business expense and it is to be debited in the books of business. (2) Received 100 bucks as interest on our fixed deposit, here interest which is received is business income and therefore it is to be credited in the books of business.

The above all are the three golden rules of accounting with examples.

**Journal:**

[Business](http://www.businessdictionary.com/definition/business.html) diary in which all [financial](http://www.businessdictionary.com/definition/financial.html) [data](http://www.businessdictionary.com/definition/data.html) (taken usually from a [journal voucher](http://www.businessdictionary.com/definition/journal-voucher.html)) pertaining to the [day](http://www.businessdictionary.com/definition/day.html) to day [business transactions](http://www.businessdictionary.com/definition/business-transaction.html) of a firm is recorded [using](http://www.businessdictionary.com/definition/user.html) [double-entry bookkeeping](http://www.businessdictionary.com/definition/double-entry-bookkeeping.html) [system](http://www.businessdictionary.com/definition/system.html). [Debit](http://www.businessdictionary.com/definition/debit.html) and [credit](http://www.businessdictionary.com/definition/credit.html) [changes](http://www.businessdictionary.com/definition/changes.html) caused by each transaction in [individual](http://www.businessdictionary.com/definition/individual.html) [ledger-accounts](http://www.businessdictionary.com/definition/ledger-account.html) are [subsequently](http://www.businessdictionary.com/definition/subsequently.html) entered in (posted to) the firm's [general ledger](http://www.businessdictionary.com/definition/general-ledger.html). Depending on the nature of its [operations](http://www.businessdictionary.com/definition/operations.html) and number of [daily](http://www.businessdictionary.com/definition/daily.html) [transactions](http://www.businessdictionary.com/definition/transaction.html), a firm may keep several [types](http://www.businessdictionary.com/definition/type.html) of specialized journals such as [cash journal](http://www.businessdictionary.com/definition/cash-journal.html) ([cash book](http://www.businessdictionary.com/definition/cash-book.html)), [purchases journal](http://www.businessdictionary.com/definition/purchases-journal.html), and [sales journal](http://www.businessdictionary.com/definition/sales-journal.html). The most [common](http://www.businessdictionary.com/definition/common.html) is [general journal](http://www.businessdictionary.com/definition/general-journal.html), used where no [special journal](http://www.businessdictionary.com/definition/special-journal.html) exists or in which transactions not belonging to other journals are entered (see [journal entry](http://www.businessdictionary.com/definition/journal-entry.html)). Journals are also [called](http://www.businessdictionary.com/definition/call.html) '[books](http://www.businessdictionary.com/definition/books.html) of first [entry](http://www.businessdictionary.com/definition/entry.html)' or '[books of original entry](http://www.businessdictionary.com/definition/books-of-original-entry.html).' See also [journalizing](http://www.businessdictionary.com/definition/journalizing.html).

# Journal entry:

The [recording](http://www.businessdictionary.com/definition/recording.html) of [financial](http://www.businessdictionary.com/definition/financial.html) [data](http://www.businessdictionary.com/definition/data.html) (taken usually from a [journal voucher](http://www.businessdictionary.com/definition/journal-voucher.html)) pertaining to [business transactions](http://www.businessdictionary.com/definition/business-transaction.html) in a [journal](http://www.businessdictionary.com/definition/journal.html) such that the [debits](http://www.businessdictionary.com/definition/debit.html) equal [credits](http://www.businessdictionary.com/definition/credit.html). Journal entries [provide](http://www.businessdictionary.com/definition/provide.html) an [audit trail](http://www.businessdictionary.com/definition/audit-trail.html) and a [means](http://www.businessdictionary.com/definition/mean.html) of analyzing the effects of the [transactions](http://www.businessdictionary.com/definition/transaction.html) on an [organization's](http://www.businessdictionary.com/definition/organization.html) [financial position](http://www.businessdictionary.com/definition/financial-position.html). See also [journalizing](http://www.businessdictionary.com/definition/journalizing.html).  
  
**Ledger:**

[Collection](http://www.businessdictionary.com/definition/collection.html) of an entire [group](http://www.businessdictionary.com/definition/group.html) of similar [accounts](http://www.businessdictionary.com/definition/accounts.html) in [double-entry bookkeeping](http://www.businessdictionary.com/definition/double-entry-bookkeeping.html). Also [called](http://www.businessdictionary.com/definition/call.html) book of final [entry](http://www.businessdictionary.com/definition/entry.html), a ledger [records](http://www.businessdictionary.com/definition/record.html) [classified](http://www.businessdictionary.com/definition/classified.html) and summarized [financial information](http://www.businessdictionary.com/definition/financial-information.html) from [journals](http://www.businessdictionary.com/definition/journal.html) (the '[books](http://www.businessdictionary.com/definition/books.html) of first entry') as [debits](http://www.businessdictionary.com/definition/debit.html) and [credits](http://www.businessdictionary.com/definition/credit.html), and shows their [current](http://www.businessdictionary.com/definition/current.html) [balances](http://www.businessdictionary.com/definition/balance.html). In [manual](http://www.businessdictionary.com/definition/manual.html) [accounting systems](http://www.businessdictionary.com/definition/accounting-system.html), a ledger is usually a loose leaf [binder](http://www.businessdictionary.com/definition/binder.html) with a separate page for each [ledger account](http://www.businessdictionary.com/definition/ledger-account.html). In computerized [systems](http://www.businessdictionary.com/definition/system.html), it consists of interlinked [digital](http://www.businessdictionary.com/definition/digital.html) [files](http://www.businessdictionary.com/definition/file.html), but follows the same [accounting principles](http://www.businessdictionary.com/definition/accounting-concepts.html) as the manual system.

# Books of account:

# The [financial](http://www.investorwords.com/5572/financial.html) [records](http://www.investorwords.com/4094/record.html), [ledgers](http://www.investorwords.com/2754/ledger.html) and [journals](http://www.investorwords.com/2674/journal.html) that [make up](http://www.investorwords.com/10259/make_up.html) the [accounts](http://www.investorwords.com/42/account.html) of a company. A [company's](http://www.investorwords.com/992/company.html) [books](http://www.investorwords.com/544/books.html) of account, or "books", represent the financial memory of the company, and are crucial for continuity, decision-making, [analysis](http://www.investorwords.com/208/analysis.html) of company [performance](http://www.investorwords.com/3665/performance.html), and ensuring regulatory [compliance](http://www.investorwords.com/5468/compliance.html).

# Cash book:

# [Journal](http://www.businessdictionary.com/definition/journal.html) in which all [cash receipts](http://www.businessdictionary.com/definition/cash-receipt.html) and [payments](http://www.businessdictionary.com/definition/payment.html) (including [bank](http://www.businessdictionary.com/definition/bank.html) [deposits](http://www.businessdictionary.com/definition/deposit.html) and withdrawals) are recorded first, in chronological [order](http://www.businessdictionary.com/definition/order.html), for [posting](http://www.businessdictionary.com/definition/posting.html) to [general ledger](http://www.businessdictionary.com/definition/general-ledger.html). [Cash](http://www.businessdictionary.com/definition/cash.html) book is regularly reconciled with the [bank statements](http://www.businessdictionary.com/definition/bank-statement.html) as an internal [auditing](http://www.businessdictionary.com/definition/audit.html) [measure](http://www.businessdictionary.com/definition/measure.html). In larger firms, it is commonly divided into two [parts](http://www.businessdictionary.com/definition/part.html): (1) [Cash disbursement journal](http://www.businessdictionary.com/definition/cash-disbursement-journal.html) in which all [cash payments](http://www.businessdictionary.com/definition/cash-payment.html) (such as [accounts payable](http://www.businessdictionary.com/definition/accounts-payable-A-P.html), [operating expenses](http://www.businessdictionary.com/definition/operating-expenses.html), [petty cash](http://www.businessdictionary.com/definition/petty-cash.html) [purchases](http://www.businessdictionary.com/definition/purchase.html)) are recorded, and (2)[Cash receipts journal](http://www.businessdictionary.com/definition/cash-receipts-journal.html) in which all cash receipts (such as [accounts receivable](http://www.businessdictionary.com/definition/accounts-receivable-A-R.html), cash [sales](http://www.businessdictionary.com/definition/sales.html), [sale of assets](http://www.businessdictionary.com/definition/sale-of-assets.html)) are recorded.

# Petty Cash Book:

It is another Cash Book which is maintained, generally, in large business concerns to reduce the burden of 'Main Cash Book', in which numerous transactions involving petty (small) amounts are recorded. For this purpose, a Petty Cashier is appointed by the Chief Cashier. The Chief Cashier advances a sum of money to the Petty Cashier to enable him to meet petty expenses for a fixed period. The Petty Cashier will record this amount on the Debit Side of the Petty Cash Book while the Chief Cashier will record the same amount on the Credit Side of the Main Cash Book.  
 The fundamental difference between the Main Cash Book and the Petty Cash Book is that only petty expenses are recorded in the Petty Cash Book. No receipt (with the exception of money received from the Chief Cashier), however small it may be, is recorded in it. But in the main Cash Book all receipts (big and small) and large expenses are recorded.

**Trial Balance:**

A bookkeeping worksheet in which the balances of all ledgers are compiled into [debit](http://www.investopedia.com/terms/d/debit.asp) and credit columns. A company prepares [a trial balance](http://www.investopedia.com/video/play/trial-balance/) periodically, usually at the end of every reporting period. The general purpose of producing a trial balance is to ensure the entries in a company's bookkeeping system are mathematically correct.

**Trading Account:**

## Definition and Explanation:

The account which is prepared to determine the gross profit or gross loss of a business concern is called trading account.

It should be noted that the result of the business determined through trading account is not true result. The true result is the net profit or the net loss which is determined through profit and loss account. The trading accounting has the following features:

1. It is the first stage of final accounts of a trading concern.
2. It is prepared on the last day of an accounting period.
3. Only direct revenue and [direct expenses](http://www.accountingexplanation.com/expenses_direct_and_indirect_expenses.htm) are considered in it.
4. Direct expenses are recorded on its debit side and direct revenue on its credit side.
5. All items of direct expenses and direct revenue concerning current year are taken into account but no item relating to past or next year is considered in it.
6. If its credit side exceeds it represents gross profit and if debit side exceeds it shows gross loss.

**Profit & Loss (P&L) Statement**

The [profit](http://www.investinganswers.com/node/2042) **& loss (P&L) statement** is one of the three primary [financial statements](http://www.investinganswers.com/node/2293) used to assess a company’s performance and financial position (the two others being the [balance sheet](http://www.investinganswers.com/node/1083) and the [cash flow statement](http://www.investinganswers.com/node/2786)). 

HOW IT WORKS (EXAMPLE):

The [profit](http://www.investinganswers.com/node/2042) *& loss statement* summarizes the [revenues](http://www.investinganswers.com/node/5108) and expenses generated by the company over the entire reporting period. The profit & loss statement is also known as the [income statement](http://www.investinganswers.com/node/1104), statement of [earnings](http://www.investinganswers.com/node/1514), [statement of operations](http://www.investinganswers.com/node/2371), or [statement of income](http://www.investinganswers.com/node/2372).

The basic equation on which a profit & loss statement is based is Revenues – Expenses= Profit.

All companies need to generate revenue to stay in business. Revenues are used to pay expenses, interest payments on [debt](http://www.investinganswers.com/node/5752), and [taxes](http://www.investinganswers.com/node/4567) owed to the government. After the costs of doing business are paid, the amount left over is called [net income](http://www.investinganswers.com/node/808). Net income is theoretically available to shareholders, though instead of paying out dividends, the firm’s management often chooses to retain earnings for future [investment](http://www.investinganswers.com/node/4904) in the business

# Balance sheet

A [condensed](http://www.businessdictionary.com/definition/condensed.html) [statement](http://www.businessdictionary.com/definition/statement.html) that shows the [financial](http://www.businessdictionary.com/definition/financial.html) position of an [entity](http://www.businessdictionary.com/definition/entity.html) on a specified date (usually the [last](http://www.businessdictionary.com/definition/Last.html) [day](http://www.businessdictionary.com/definition/day.html) of an [accounting period](http://www.businessdictionary.com/definition/accounting-period.html)).

Among other [items](http://www.businessdictionary.com/definition/item.html) of [information](http://www.businessdictionary.com/definition/information.html), a balance sheet [states](http://www.businessdictionary.com/definition/state.html) (1) what [assets](http://www.businessdictionary.com/definition/asset.html) the entity owns, (2) how it [paid for](http://www.businessdictionary.com/definition/paid-for.html) them, (3) what it owes (its [liabilities](http://www.businessdictionary.com/definition/liability.html)), and (4) what is the [amount](http://www.businessdictionary.com/definition/amount.html) left after satisfying the liabilities. Balance sheet [data](http://www.businessdictionary.com/definition/data.html) is based on a [fundamental](http://www.businessdictionary.com/definition/fundamental.html) [accounting equation](http://www.businessdictionary.com/definition/accounting-equation.html) (assets = liabilities + [owners' equity](http://www.businessdictionary.com/definition/owners-equity.html)), and is [classified](http://www.businessdictionary.com/definition/classified.html) under subheadings such as [current assets](http://www.businessdictionary.com/definition/current-asset.html), [fixed assets](http://www.businessdictionary.com/definition/fixed-asset.html), [current liabilities](http://www.businessdictionary.com/definition/current-liabilities.html), [Long-term](http://www.businessdictionary.com/definition/long-term.html) Liabilities.

With [income statement](http://www.businessdictionary.com/definition/income-statement.html) and [cash flow statement](http://www.businessdictionary.com/definition/cash-flow-statement.html), it [comprises](http://www.businessdictionary.com/definition/comprise.html) the set of [documents](http://www.businessdictionary.com/definition/documents.html) indispensable in running a [business](http://www.businessdictionary.com/definition/business.html). An audited balance sheet is often demanded by [investors](http://www.businessdictionary.com/definition/investor.html), [lenders](http://www.businessdictionary.com/definition/lender.html), [suppliers](http://www.businessdictionary.com/definition/supplier.html), and [taxation](http://www.businessdictionary.com/definition/taxation.html) [authorities](http://www.businessdictionary.com/definition/authority.html); and is usually [required](http://www.businessdictionary.com/definition/required.html) by [law](http://www.businessdictionary.com/definition/law.html). To be considered [valid](http://www.businessdictionary.com/definition/valid.html), a balance sheet must give a [true and fair view](http://www.businessdictionary.com/definition/true-and-fair-view.html) of an[organization's](http://www.businessdictionary.com/definition/organization.html) state of affairs, and must follow the [provisions](http://www.businessdictionary.com/definition/provision.html) of [GAAP](http://www.businessdictionary.com/definition/generally-accepted-accounting-principles-GAAP.html) in its [preparation](http://www.businessdictionary.com/definition/preparation.html). Also [called](http://www.businessdictionary.com/definition/call.html) statement of [condition](http://www.businessdictionary.com/definition/condition.html), statement of [financial condition](http://www.businessdictionary.com/definition/financial-position.html), or statement of financial position.

**Income Statement**

**DEFINITION of 'Income Statement'**

A financial statement that measures a company's [financial performance](http://www.investopedia.com/terms/f/financialperformance.asp) over a specific [accounting period](http://www.investopedia.com/terms/a/accountingperiod.asp). Financial performance is assessed by giving a summary of how the business incurs its [revenues](http://www.investopedia.com/terms/r/revenue.asp) and expenses through both operating and non-operating activities. It also shows the net profit or loss incurred over a specific accounting period, typically over a fiscal quarter or year.

Also known as the "profit and loss statement" or "statement of revenue and expense."

**Gross Profit**

A company's total revenue (equivalent to total sales) minus the cost of goods sold. Gross profit is the profit a company makes after deducting the costs associated with making and selling its products, or the costs associated with providing its services. Gross profit will appear on a company's income statement or can be calculated with this formula:

Gross profit = revenue - cost of goods sold

Also called "gross margin," "sales profit" and "gross income".

**Net Profit:**

Net profit, also referred to as the bottom line, net income, or net earnings is a measure of the profitability of a venture after accounting for all costs. In a survey of nearly 200 senior marketing managers, 91% responded that they found the "net profit" metric very useful.[[1]](https://en.wikipedia.org/wiki/Net_profit#cite_note-Marketing_Metrics-1) In [accounting](https://en.wikipedia.org/wiki/Accountancy), net profit is equal to the [gross profit](https://en.wikipedia.org/wiki/Gross_profit) minus [overheads](https://en.wikipedia.org/wiki/Overhead_(business)) minus [interest](https://en.wikipedia.org/wiki/Interest) payable for a given time period (usually: [accounting period](https://en.wikipedia.org/wiki/Accounting_period)).[[citation needed](https://en.wikipedia.org/wiki/Wikipedia:Citation_needed)]

A common synonym for "net profit" when discussing [financial statements](https://en.wikipedia.org/wiki/Financial_statements) (which include a [balance sheet](https://en.wikipedia.org/wiki/Balance_sheet) and an [income statement](https://en.wikipedia.org/wiki/Income_statement)) is the [bottom line](https://en.wikipedia.org/wiki/Bottom_line). This term results from the traditional appearance of an income statement which shows all allocated revenues and expenses over a specified time period with the resulting summation on the bottom line of the report.

**Retained Earnings**

DEFINITION of 'Retained Earnings'

Retained earnings is the percentage of [net earnings](http://www.investopedia.com/terms/n/netincome.asp) not paid out as [dividends](http://www.investopedia.com/terms/d/dividend.asp), but retained by the company to be reinvested in its core business, or to pay debt. It is recorded under [shareholders' equity](http://www.investopedia.com/terms/s/shareholdersequity.asp) on the [balance sheet](http://www.investopedia.com/terms/b/balancesheet.asp).The formula calculates retained [earnings](http://www.investopedia.com/terms/e/earnings.asp) by adding net income to (or subtracting any net losses from) beginning retained earnings and subtracting any dividends paid to shareholders:

Retained Earnings (RE) = Beginning RE + Net Income – Dividends

Also known as the "retention ratio" or "retained surplus".

**Accounts Receivable Journal Entries**

The accounts receivable journal entries below act as a quick reference, and set out the most commonly encountered situations when dealing with the double entry posting of [accounts receivable](http://www.double-entry-bookkeeping.com/debtors/debtors/).

In each case the accounts receivable journal entries show the debit and credit account together with a brief narrative. For a fuller explanation of journal entries, view our [examples](http://www.double-entry-bookkeeping.com/double-entry-bookkeeping-example/) section.

Typical Accounts Receivable Journal Entries

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Accounts receivable | XXX |  |
| Revenue |  | XXX |
| To record a sale to an account customer | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Cash | XXX |  |
| Accounts receivable |  | XXX |
| To receive a cash payment from an account customer | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Cash | XXX |  |
| Discount allowed | XXX |  |
| Accounts receivable |  | XXX |
| To receive a cash payment from an account customer taking cash discount | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Revenue | XXX |  |
| Accounts receivable |  | XXX |
| A credit note is issued to a customer | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Bad debt expense | XXX |  |
| Accounts receivable |  | XXX |
| To write off an accounts receivable as a bad debt | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Bad debt expense | XXX |  |
| Allowance for doubtful debts |  | XXX |
| To set up an allowance for doubtful debts | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Allowance for doubtful debts | XXX |  |
| Accounts receivable |  | XXX |
| To use the allowance for doubtful debts to write off an accounts receivable | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Cash | XXX |  |
| Accounts receivable |  | XXX |
| Accounts receivable | XXX |  |
| Allowance for doubtful debts |  | XXX |
| To record cash received after an accounts receivable has been written off | | |

**Accounts Payable Journal Entries**

The accounts payable journal entries below act as a quick reference, and set out the most commonly encountered situations when dealing with the double entry posting of [accounts payable](http://www.double-entry-bookkeeping.com/category/creditors/).

In each case the accounts payable journal entries show the debit and credit account together with a brief narrative. For a fuller explanation of journal entries, view our [examples](http://www.double-entry-bookkeeping.com/double-entry-bookkeeping-example/) section.

[Home](http://www.double-entry-bookkeeping.com/) » [Accounts Payable](http://www.double-entry-bookkeeping.com/category/accounts-payable/) » Accounts Payable Journal Entries

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Purchases | XXX |  |
| Accounts payable |  | XXX |
| To record a purchase on account from a supplier | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Accounts payable | XXX |  |
| Cash |  | XXX |
| To make a cash payment to an account supplier | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Accounts payable | XXX |  |
|  |  |  |
| Discount received |  | XXX |
| Cash |  | XXX |
| To make a cash payment taking a supplier early settlement discount | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Accounts payable | XXX |  |
| Purchases |  | XXX |
| Goods returned and a debit note is issued to a supplier | | |

|  |  |  |
| --- | --- | --- |
| Account | Debit | Credit |
| Accounts payable | XXX |  |
| Notes payable |  | XXX |
| Notes payable issued to replace an accounts payable | | |

# 