Debit and Credit

by Sophia

WHAT'S COVERED

This tutorial will cover the topic of debits and credits, focusing on what the terms mean and how they apply to account groups.

Our discussion breaks down as follows:

1. Basic Accounting Equation

Before we begin discussing debits and credits, it is important to set the stage with a critical concept: the basic accounting equation. The basic accounting equation is assets equal liabilities plus owner's equity:

The most important thing to note is that this equation must *always* balance. Keep this in the back of your mind during the discussion of debits and credits; when reviewing the different debits and credits within the accounts, make sure that this equation is always in balance.

BIG IDEA

Remember, assets must always equal liabilities plus owner's equity.

1a. Account Groups Review

Each account is a member of one of the account groups. Each account provides a greater level of detail for the resources impacted within the account groups.

Account Group	Account
Asset	Cash Accounts Receivable Supplies Long Term Assets

Liability	Accounts Payable Notes Payable Utilities Payable
Equity	Equity Owner's Withdrawals
Revenue	Service Revenue Rent Revenue
Expense	Wages Expense Utilities Expense Advertising Expense

2. Debit and Credit

Now we are ready to discuss debits and credits, starting with debits. A**debit** is an entry that is made on the left side of an account. A **credit**, on the other hand, is an entry made on the right side of an account.

HINT

Remember, debits are on the left, and credits are on the right.

Now, why do we use debits and credits? Well, debits and credits are used to show monetary changes within individual accounts. They help to keep a detailed record of all the increases and decreases within accounts, account groups, and financial statements. So, debits and credits can either be increases or decreases; it simply depends on the type of account.

Account Group	Debit	Credit
Asset	Increases	Decreases
Liability	Decreases	Increases
Equity	Decreases	Increases
Revenue	Decreases	Increases
Expense	Increases	Decreases

Circling back to the accounting equation, another thing to remember about debits and credits is that in total, your debits must always equal your credits. This is very important when you are looking at entries within your specific accounts: *the debits in total must always equal the credits in total*

TERMS TO KNOW

Debit

Entry made on the left side of an account.

Credit

Entry made on the right side of an account.

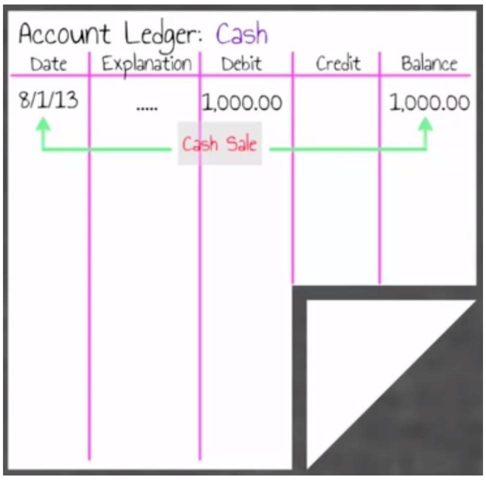
3. Examples of Accounting Events

3a. Cash Sale

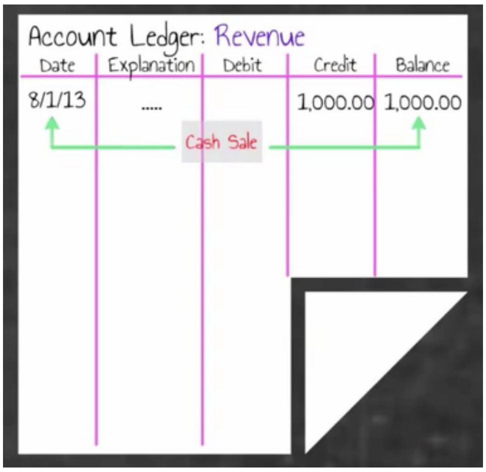
If you have a cash sale in your business, there will be two accounts impacted:

- Assets impacted for the cash
- Revenue impacted for the sale.

Let's look at the assets, or cash, first. What's going to happen to cash? Well, you're going to have a transaction that takes place--a cash sale--on any given date that this happens. You're going to put that debit into the cash account, because you're receiving cash for the sale; therefore, your cash is going up.



Now, let's look at the revenue. Remember, you had $1,000 cash debit, so you're also going to credit revenue for $1,000. Again, your total debits equal your total credits for that cash sale.

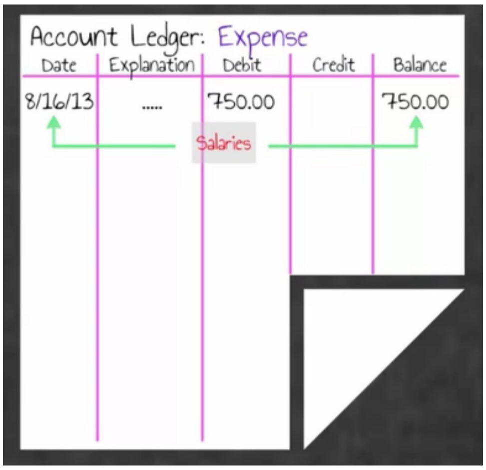


3b. Salaries

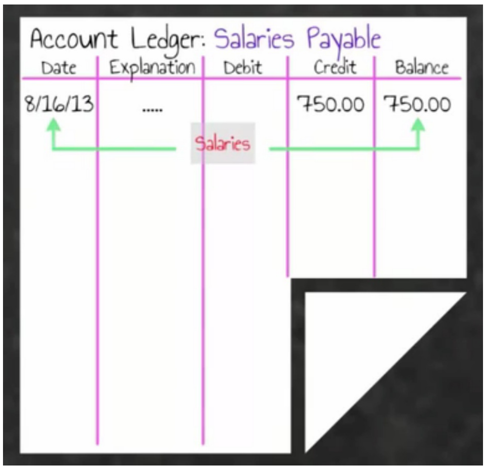
Our next example involves salaries. There will be two accounts impacted:

- Expenses for the expense that you're incurring
- Liabilities for the money that you owe

Starting with the expenses, if you look at your expense account for salaries, you'll see a debit to that expense, because debits increase your expenses.



Next, you'll need to have a corresponding credit, and that credit is to your liabilities. In other words, it's money that you owe. If you look at your salaries payable for the salaries that you owe, you will see a credit in that salaries payable. Once again, your total debits of $750 equal your total credits of $750.

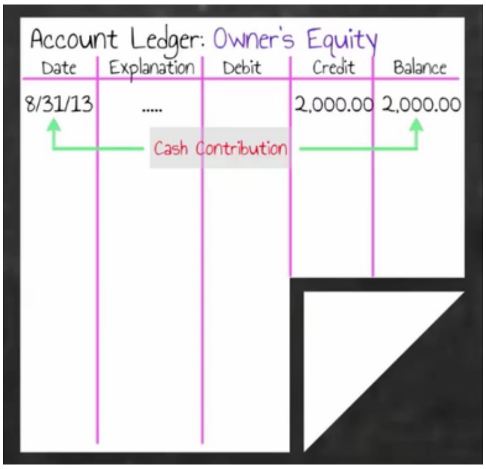


3c. Owner Contribution

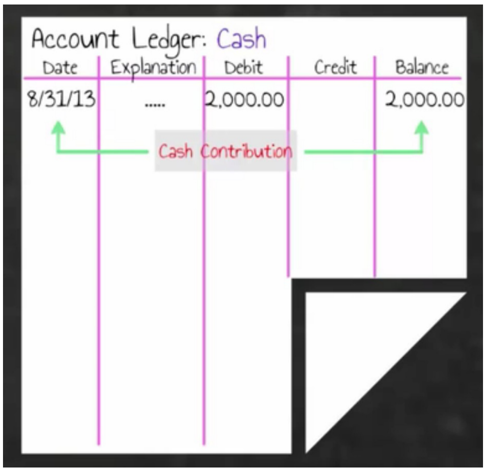
Suppose you are an owner who is contributing cash to a business. There will be two accounts impacted:

- Equity
- Cash

Starting with the equity, if you look at your owner's equity account for a cash contribution, what will you see? You'll see a credit to owner's equity, because you, the owner, are contributing cash, so your equity is growing--and equity is increased through credits.



It follows, then, that you will see a corresponding debit of equal value. In the image below, you can see that cash came in. You received cash from that contribution, so your cash is debited for $2,000--and your total debits of $2,000 equal your total credits.



SUMMARY

Today we learned about the **basic accounting equation**: assets equal liabilities plus owner's equity. This is an important concept to understand when setting the framework for **debits and credits**, which we also discussed. In total, debits and credits must always equal, as illustrated in our **examples of accounting events**.

Source: Adapted from Sophia instructor Evan McLaughlin.

TERMS TO KNOW

Credit
Entry made on the right side of an account.

Debit
Entry made on the left side of an account.

