**ACCOUNTING BASICS – DEFINITIONS OF COMMON ACCOUNTING TERMS.**

**Accounts**  
Accounts are simply established to provide a record of individual business transactions as they apply to a certain area or item. Your personal checking account is established in order to provide a record of individual personal financial transactions you create when you write a check. All of the accounts are listed in a general ledger. Today, the actual ledger book has long since been replaced by accounting software that creates a general ledger on the computer. The concept however has not been altered.   
  
The **general ledger** is the central location for maintaining all your accounts.

**Journal entries** refer to the posting or entering of the financial transactions to a particular account.  
  
**Assets, Liabilities, Equity, Revenue and Expenses**  
**Assets** are accounts that add value to your individual or business worth.

**Liabilities** are accounts that remove value from your individual or business worth.

**Equity** is used to identify the individual contribution of money, or other financial equivalent, invested in individual or business worth.

The **revenue** account is simply the account that tracks all income generated.

The **expense** accounts are the individual accounts setup to record the financial transactions that occur, as expenditure, in generating that income.

***Practical application of accounting accounts:*** An example of an asset would be your car. Your car has a dollar value attached to it. It adds value to your individual worth. An example of a liability would be your car loan. The loan removes value from your individual worth. The equity in your car would be any money you paid down toward the purchase. If you use your car to operate a pizza delivery service, the income generated from delivering pizzas would be known as revenue. Any expense for gas or car repairs would be recorded in an expense account known as “automotive expense”.

**Debits and Credits**  
Every single transaction recorded in the accounting process falls into one of two categories: it is either a debit or a credit. A debit is a transaction of value “added” to an account. A credit is a transaction of value “removed” from an account. Debit, value is added. Credit, value is removed.   
  
In a general ledger or accounting journal, Debits are always in the left column and credits occupy the right. For example;

Reed Inc. borrowed $50,000.

Cash (debit account) 50,000

Accounts payable 50,000

Generally, Asset accounts like cash, accounts receivable, inventory, etc are debit accounts. This means that when they increase, they are debited and when they decrease they are credited. Gaining an asset always results in a debit entry.

Liability accounts like accounts payable, notes payable, interest payable, etc. are credit accounts. When they increase, they are credited and when they decrease they are debited.

Equity accounts have two facets: Revenue and expense.

Revenue accounts are credit accounts and expenses are debit accounts. When a company receives money for its goods or services, the revenue accounts increase and when the company incurs an expense, the expense account increases.

Example:

Reed received $2000 for its goods.

Cash 2000

Revenue 2000

Reed paid rent of $4000

Rent expense 4000

Cash 4000

Note that all entries for transactions have two sides – A debit and a credit. In accounting, every single transaction must have a debit and credit side and they must be equal.