CLASSES
BY
SACHIN SHARMA

BE EXTRAORDINARY

CALL AT 9891397427

What is ACCOUNTS?

Explaining Accounts through an example.

Lets first understand the concept of Redlight.
Q: What does a Redlight do on the road?
A: It allows the smooth flow of traffic.

Q: What will happen if the redlights are stopped working for a while?
A: There will be a total chaos on the road. There could be n number of accidents as everybody wants to cross the road.

Same is the relationship of Accounts with respect to a business as the redlight is meant for the traffic.

What is ACCOUNTS?

Q: What does Accounts do?
A: It helps the business owner to understand its finances. How much cash he has currently, where does he has spent his cash. From whom he has purchased goods, on what day, in what amount, how much he has paid to the suppliers, what's the balance left and so on.

By maintaining our Accounts, we have answers to n no. of questions while if we don't maintain accounts, we have just the questions not just from us but from the various parties with whom we have dealt with absolutely NO ANSWERS.

What is ACCOUNTS?

Accounts is **that system** through which we get information about

- How much we have earned at the end of the year
- What are our liabilities that we need to settle
- From whom we need to receive the amount
- What were our expenses and the amount of each of them
- And various other information that we need

So from where does our Accounts Start?

There are transactions that happen in the business on daily basis like paying salary to employees, paying the rent of a business, buying good, selling goods, withdrawing cash from the bank.

Accounts STARTS with
PASSING THE JOURNAL ENTRY for these VARIOUS TRANSACTIONS.

What’s the Journal Entry

Journal entry is the way to record these transactions. This is the first step and the foundation through which the accounts started. If the journal entry is passed following the rules of the journal entries, the foundation of Accounts is built.

To understand Journal entry, we need to first understand the components of the journal entries.

There are 4 components of Journal entry.
Assets, Liabilities, Expenses and Income.

ASSETS are what a company owns.

It includes all the resources a company has at its disposal/use: namely, the Cash, Bank balance, Building, Furniture, Machinery, Vehicles, Stock in hand, Amount to be collected from the goods sold on credit etc.

LIABILITIES are any amount that is owed to others.

It includes loans that must be paid back, any amount that is owed for goods bought on credit, any expense that has not yet been paid.

EXPENSES:
It means and includes day to day expenses that the business do. For Eg. Goods purchased, Rent paid, Salary paid etc.

INCOME:
It means the earnings/ Income of the business through sale of goods or services.

There are certain rules with respect these **4 components** to record journal entries and the rules are as follows:-

RULES FOR PASSING JOURNAL ENTRY:

ASSET

Dr.	Cr.
+	-
Increase in ASSETS	Decrease in ASSETS

LIABILITY

Dr.	Cr.
-	+
Decrease in Liability	Increase in Liabilty

EXPENSES

Dr.	
+	
Always Debited	

INCOME

	Cr.
	-
	Always Credited

Now using the above rules, I am explaining how to record the following transactions through Journal Entry.

1. Paid rent for the shop 25,000
2. Paid salary for the employee 15,000
3. Purchased goods costing 20,000 on cash
4. Purchased goods costing 20,000, payment made though cheque.
5. Sold goods for 50,000, payment received half on cash, half through cheque
6. Purchased Furniture for Rs. 20,000

This is the way to write Journal Entry

1	**Paid Rent**	
	Rent A/c Dr. (Expenses always **Debited**)	**Debit**
	To Cash A/c (Asset is decreasing So **Credited**)	**Credit**
2	**Paid Salary**	
	Salary A/c Dr. (Expenses always **Debited**)	**Debit**
	To Cash A/c (Asset is decreasing So **Credited**)	**Credit**
3	**Purchased goods**	
	Purchases A/c Dr. (Purchases is always an Expenses so always **Debited**	**Debit**
	To Cash A/c (Cash, Asset is decreasing so **Credited**)	**Credit**
4	**Purchased goods**	
	Purchases A/c Dr.	**Debit**
	To Bank A/c (Bank, Asset is decreasing so **Credited**)	**Credit**

5	**Good were sold**
	Cash A/c Dr. (Asset is Increasing So **Debited**)
	Bank A/c Dr. (Asset is Increasing So **Debited**)
	To Sales A/c (Income always **Credited**)
6	**Purchased Furniture**
	Furniture A/c Dr. (Asset is Increasing So **Debited**)
	To Cash A/c (Asset is decreasing So **Credited**)

Journal Entry with Amount

1	**Paid Rent**		
	Rent A/c Dr. (Expenses always **Debited**)	25,000	
	To Cash A/c (Asset is decreasing So **Credited**)		25,000
2	**Paid Salary**		
	Salary A/c Dr. (Expenses always **Debited**)	20,000	
	To Cash A/c (Asset is decreasing So **Credited**)		20,000
3	**Purchased goods**		
	Purchases A/c Dr. (Pur. is always an Exp. so always **Debited**	20,000	
	To Cash A/c (Cash, Asset is decreasing so **Credited**)		20,000
4	**Purchased goods**		
	Purchases A/c Dr.	20,000	
	To Bank A/c (Bank, Asset is decreasing so **Credited**)		20,000

Journal Entry with Amount

5	**Good were sold**		
	Cash A/c Dr. (Asset is Increasing So **Debited**)	25,000	
	Bank A/c Dr. (Asset is Increasing So **Debited**)	25,000	
	To Sales A/c (Income always **Credited**)		50,000
6	**Purchased Furniture**		
	Furniture A/c Dr. (Asset is Increasing So **Debited**)	20,000	
	To Cash A/c (Asset is decreasing So **Credited**)		20,000

What will happen if a wrong Journal entry is passed:-

Salary paid
Correct entry is:-
Salary A/c Dr.
    To Cash A/c

But Entry passed was
Cash A/c Dr.
    To Salary A/c

Now Salary is an expense but in our books, we considered it as an Income due to which our profit will increase as we have shown an expense as an income.

Also our cash is decreasing but we have increased our cash
due to which our actual cash will not match with what is there in our books.

What does Debit and Credit means

Debit means the Left side of the T-account

and

Credit means the Right side of the T-account.

Debit and Credit also the plus and the minus of that respective item.

For Eg. While passing Journal entry, For Cash (Asset), Debit means that Cash is increased while Credit means that Cash is decreased.

For liability it's the other way.

Expenses are always Debited and Income are always Credited.

LET’S REVISE

Accounting is the process of recording **FINANCIAL** transactions pertaining to a **BUSINESS**.

Note:

- **Only** Financial transactions are to be recorded. Non financial transactions (i.e. transactions which are not in money terms are not to be recorded in Accounts)
- We use Accounts in business **only**.

ACCOUNTS IS A PROCESS

It starts with

- Recording of each transaction through journal entry
- Then preparing ledger accounts for each account used in journal entry
- Then preparing the trial balance which is the summary of the closing balances of the ledger
- Based on the trial balance our final accounts are prepared through which we came to know how much profit we have earned and what is our position.

1. Transactions

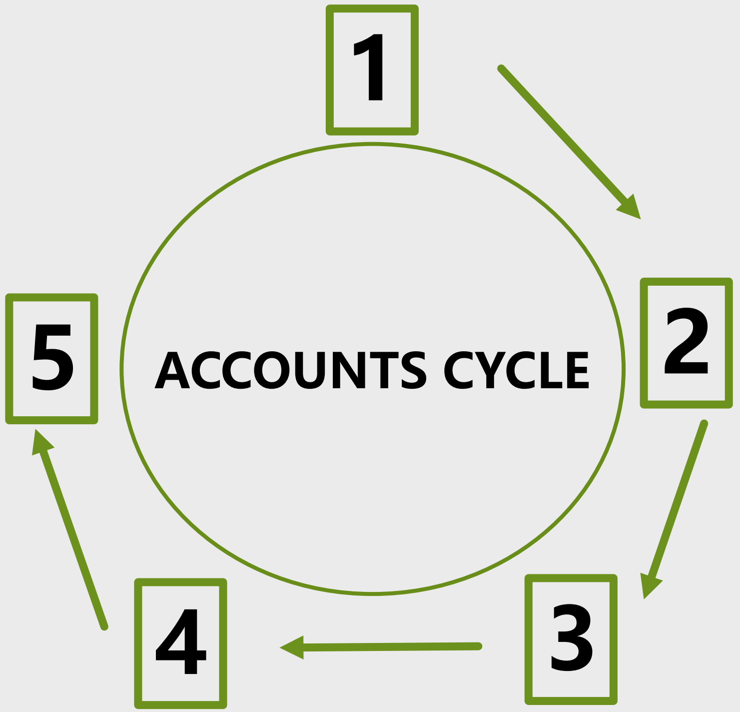
2. Journal entry

3. Ledger A/c

4. Trial Balance

5. Final Accounts

Flow of Accounting Cycle.



Transactions

are what the business do on daily basis. For Eg. Purchase of goods, Sale of goods, Salary paid, Rent paid, Furniture purchased etc.

Then Journal entry

for each transaction is passed. Here we need to follow certain rules. Journal entry is the most important step in the whole Accounting cycle.

Then Ledger A/cs

are prepared for each of the Account that we have used while passing journal Entry.

The closing balances of the ledger Accounts are transferred to the **Trial Balance.**

Based on the Trial balance, our **Final Accounts** are prepared which give us the Net profit /Loss of the business during the year and Balance sheet which give us the figures of our Assets and Liabilities.

Our Transactions revolve around these 4 only:-

- ASSET
- LIABILITY
- EXPENSE
- INCOME

ASSET: An asset is **any resource owned or controlled by a business.** It is anything that can be used to produce the goods or through which the business is done.
Eg. Machinery, Furniture, Building, Cash in hand, Bank balance

LIABILITY: A liability is **something a person or company owes**, usually a sum of money.
Eg. Loan taken from Bank, Goods purchased on credit.

EXPENSE: An expense is the money spent, or costs incurred, by a business in their effort to generate revenues.
Essentially, expenses **represent the cost of doing business**; they are the sum of all the activities that hopefully generate a profit.

INCOME: Income is the revenue a business earns from selling its goods and services This is often called gross income, total sales, since it includes all the company income and sales before deducting expenses.

Another meaning of income refers to net income. Net income equals the total company revenues minus total company expenses.

LIABILITIES VS. EXPENSES

A liability is money owed to buy an asset, like a loan used to purchase new office equipment.

Expenses are ongoing payment for something that has no physical value or for a service.

RULES

FOR

PASSING

JOURNAL ENTRY

ASSET	: Dr.+ Cr. -
LIABILITY	: Dr.- Cr. +
EXPENSES	: Always Debited
INCOME	: Always Credited

ASSET

If an Asset is Increasing We will Debit that Asset

If an Asset is Decreasing We will Credit that Asset

LIABILITY

If a Liability is Increasing We will Credit that Liability

If a Liability is Decreasing We will Debit that Liability

EXPENSES

Always Debited

INCOME

Always Credited

JOURNAL ENTRY for EXPENSE

Salary paid

Salary IS AN Expense (& expenses is always DEBITED)

While paying Salary, our CASH IS DECREASING (↓)so Cash being an Asset is to be CREDITED (as decrease in asset is always credited)

So the journal entry of Salary paid is: **Salary A/c Dr.**

To Cash A/c

Similarly the entry for Rent paid is **Rent A/c Dr.**

To Cash A/c

The entry for Interest paid is **Interest A/c Dr.**

To Cash A/c

The entry for Commission paid is **Commission A/c Dr.**

To Cash A/c

Here in all the entries :-

Cash is CREDITED as the cash being an asset is decreasing.

and Rent, Interest, Commission – all are expenses – so DEBITED.

JOURNAL ENTRY for INCOME

INTEREST received

Here interest in an INCOME so it is always CREDITED

While receiving interest, CASH is INCREASING (↑)so Cash being an Asset is to be DEBITED

So the journal entry of interest received is: **CASH A/c Dr.**

To INTEREST A/c

Similarly the entry for Rent received is
CASH A/c Dr.
To RENT A/c

Similarly the entry for Commission received is
CASH A/c Dr.
To COMMISSION A/c

Here in all the entries :-
Cash is DEBITED as the cash being an asset is INCREASING (& increase of asset is always debited)
and Rent, Commission – all are INCOME (and income is ALWAYS CREDITED)

JOURNAL ENTRY for ASSET PURCHASED/SOLD

FURNITURE PURCHASED

Here Furniture is an ASSET and It is increasing so it is to be DEBITED

While purchasing Furniture, our CASH is GOING OUT/DECREASING (↓)so it is to be CREDITED

So the journal entry of FURNITURE PURCHASED is:
FURNITURE A/c Dr.
To CASH A/c

Similarly the entry for MACHINERY PURCHASED is
MACHINERY A/c Dr.

To CASH A/**c**

Similarly the entry for BUILDING PURCHASED is
BUILDING A/c Dr.

To CASH A/c

Here in all the entries :-
Cash is CREDITED as the cash being an asset is DECREASING (& decrease in asset is always credited)
and MACHINERY, BUILDING all are ASSET (and they are increasing and increase in ASSET is ALWAYS DEBITED)

JOURNAL ENTRY for LOAN TAKEN

LOAN TAKEN

Here LOAN TAKEN is a LIABILITY and It is increasing (↑)so it is to be CREDITED (as increase in liability is always credited)

While taking loan, our CASH is INCREASING (↑)so it is to be DEBITED (as **increase in ASSET is always DEBITED)**

So the journal entry of **LOAN TAKEN** is:
CASH A/c Dr.
To BANK LOAN A/c

MIXED EXAMPLES

Salary paid		**Salary : Expense (Dr.)**		**Salary A/c Dr.**
		Cash: Asset ↓ (Cr.)		**To Cash A/c**
Commission received		**Commission : Income(Cr.)**		**Cash A/c Dr.**
		Cash: Asset ↑ (Dr.)		**To Commission A/c**
Furniture purchased		**Furniture: Asset ↑** (Dr.)		**Furniture A/c Dr.**
		Cash : Asset ↓ (Cr.)		**To Cash A/c**
Cash deposited into Bank		**Bank : Asset ↑** (Dr.)		**Bank A/c Dr.**
		Cash : Asset ↓ (Cr.)		**To Cash A/c**
Rent paid		**Rent : Expense (Dr.)**		**Rent A/c Dr.**
		Cash : Asset ↓ (Cr.)		**To Cash A/c**

MIXED EXAMPLES

Goods purchased		**Purchases : Expense (Dr.)**		**Purchases A/c Dr.**
		Cash : Asset ↓ (Cr.)		**To Cash A/c**
Goods sold		Cash : Asset ↑ (Dr.)		**Cash A/c Dr.**
		Sales : Income(Cr.)		**To Sales A/c**
Machinery sold		Cash : Asset ↑ (Dr.)		**Cash A/c Dr.**
		Machinery : Asset ↓ (Cr.)		**To Machinery A/c**
Interest received		Cash: Asset ↑ (Dr.)		**Cash A/c Dr.**
		Interest : Income(Cr.)		**To Interest A/c**
Loan taken from Bank		Bank : Asset ↑ (Dr.)		**Bank A/c Dr.**
		Bank loan : Liability ↑ (Cr.)		**To Bank loan A/c**

GOODS PURCHASED AND ASSET PURCHASED- DIFFERENCE

Goods purchased is an expense. WHY?

Because these are purchased to sell them and not to be used In the business.

While the Asset we purchase is to use them in our business.

So goods purchased are to be treated like an EXPENSE and SO ALWAYS DEBITED.