**Purpose:** The purpose of this handout is to summarize some key concepts that will be used repeatedly throughout this course. Most importantly you will be introduced to t-accounts and debits and credits. A full understanding of this chapter is pivotal to your success in this course. The contents of this chapter will provide the bottom building blocks for the foundation for this course. It is very important that you commit the necessary time to this chapter. Everything we do from this day forward will involve the concepts of debits and credits.

**This chapter in perspective:**

This chapter will really be an expansion of what we have done so far. Recall that we have analyzed transactions. We determined what accounts were being utilized, decided whether we wanted to increase or decrease the account. We recorded the transaction under the proper caption. Furthermore, we insured that the equation was in balance after we recorded the transaction.

Recording transactions under columnar headings is very messy and inefficient. In this chapter, we will learn about tools used to record business transactions. This chapter will serve as a stepping-stone to the next chapter.

**T-Accounts**

T-Accounts will replace the columnar headings we have been using so far. A T-Account looks like a big T. Each account will have its own T. Depending on the type of account that we will use, increases and decreases will be recorded on the appropriate debit or credit side.

* A debit just means the left side.
* A credit just means the right side.
* You summarize a T-Account by adding up both sides and placing the balance of the account (the difference between the two sides) on the side with the larger total. This is called "footing" an account.

We will utilize T-Accounts to help us understand the five basic rules of accounting.

* One thing to keep in mind: Debits equal credits--ALWAYS!!!
“Normal Balance”  The side of the account that receives the increase.

All accounts should have normal balances.

*See rules for debits and credits on separate handout*

**Trial Balance**

- Prepared after transactions have been recorded.
- All accounts should have normal balances.
- Purpose is to prove equality of debits and credits.
- If the Trial Balance totals are not equal, the financial statements will not balance.
- If the Trial Balance totals do not equal, try the following:
  1. Look for balances that are not normal.  
  2. Check the transfer of totals from T-Accounts to the Trial Balance.  
  3. Re-add the columns.  
  4. Re-compute the account totals.  
  5. Look for the total difference, half the difference, or double the difference.  
  6. If the difference is divisible by 9, then you most likely have a transposition error or a slide error.

**Financial Statements**

The result of the summarizing process of accounting.

All financial statements are inter-connected; therefore, the order of preparation is important.

Headings are important:

Each financial statement has a three-part heading

- Name of the Company

- Name of the Statement

- Time period covered - or date

Dollar signs, total lines, and double-ruled lines are important.

These go out to external users. The appearance is important.
Three financial statements that we will learn and expand upon during the semester:

1. Income Statement
2. Statement of Owner's Equity
3. Balance Sheet

(See previous chapter notes. Again, STUDY THESE as we will use them in every chapter from here on out.)

**Chart of Accounts**
A chart of accounts is a list of all the accounts that a business uses. Accounts are assigned numbers based on the type of account. No matter how many digits are included in an account number, all companies keep a uniform numbering system where all assets begin with a 1, all liabilities begin with a 2, all equity accounts begin with a 3, all revenue accounts begin with a 4 and all expense accounts begin with a 5. An example of a typical numbering system can be found in your text.

**Permanent and Temporary Accounts**
All accounts are either considered permanent or temporary....one or the other. Accounts that have balances that are carried forward from one period to the next are called permanent or real accounts. These would include asset, liability, and owner's equity accounts (except for drawing.) In other words, all BALANCE SHEET accounts are considered real or permanent.

Temporary accounts, on the other hand, are temporary which means they must start over at the beginning of the next period. These are also known as nominal accounts. Revenue and expense accounts, along with the drawing account, are considered nominal or temporary. We will discuss how closing entries work -- and how the process of closing the nominal accounts out to zero-- in the next chapter.