FINANCE AT A GLANCE

Ending balances of accounts

Lesson 46

In this lesson, we shall show how the definitions of debit and credit, that we have been using so far, affect the way an asset, a liability, and equity, an expense or a revenue ends up its balance in the accounting books.

As early as Lesson 39, we made the following definitions:

An increase in an asset is called a debit.

A decrease in an asset is called a credit.

Based on these definitions, if an asset starts with a zero balance (which is the case just before a business entity starts transacting), and the cumulative debits to the asset always outweigh the credits, then that asset has a debit balance. An asset, under usual circumstances, ends up with a debit balance as of a given point in time.

In the same lesson, we also said:

An increase in a Liability or Equity is called a credit.

A decrease in a Liability or Equity is called a debit.

If a liability or an equity starts with a zero balance (which is the case just before a business entity starts transacting), and the cumulative credits to the liability or equity always outweigh the debits, then we say that the liability or equity has a credit balance. A liability or an equity, under usual circumstances, ends up with a credit balance as of a given point in time.

Expenses and revenues, as will be shown later, are “transferred” to the Retained earnings account at the point in time when financial statements have to be drawn. After that transfer, each expense and revenue account has a zero balance. We shall be concerned with that later in the accounting process. Our concern right now is the interim point in time prior to preparing the financial statements. If the debits to an expense outweight the credits, then such expense has a debit balance. Similarly, if the credits to a revenue account outweigh the debits, the that revenue account has a credit balance, as of such interim point in time.

In summary, we can say that under normal circumstances, just prior to the preparation of financial statements, the accounting books show that:

Asset and expenses accounts have debit balances.

Liability, equity and revenue accounts have credit balances.

Until the next lesson,

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