

Training Course Fundamentals of Accounting for Non-Professionals

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Lecture 4



Lecture Outlines

- **The History of Accounting.**
- **Definition and Importance of Accounting**
- **Users of accounting**
- **Types of Accounting: Financial and Managerial**
- **Principles and Assumptions of Accounting**



Lecture

01

Introduction to Accounting

Lecture Outlines

- Understanding the Basic Equation
- Understanding the Expanded Accounting Equation
- Adjusting the accounting errors



Lecture

02

Basic and Expanded Accounting Equations

Lecture Outlines

- Recording process (journaling and posting ledgers, trial balance)
- How to Inspect Accounts and Verify the Accuracy of Financial Records



Lecture

03

Accounts and recording process

Lecture Outlines

- **Understanding the Income Statement and its Importance**
- **Understanding the Statement of Changes in Equity and its Importance**
- **Understanding the Balance Sheet and its Importance**
- **Financial position analysis and financial performance evaluation.**
- **Types of Companies Based on the Nature of Business and Ownership.**



Lecture **04**

Reports and Financial Statements

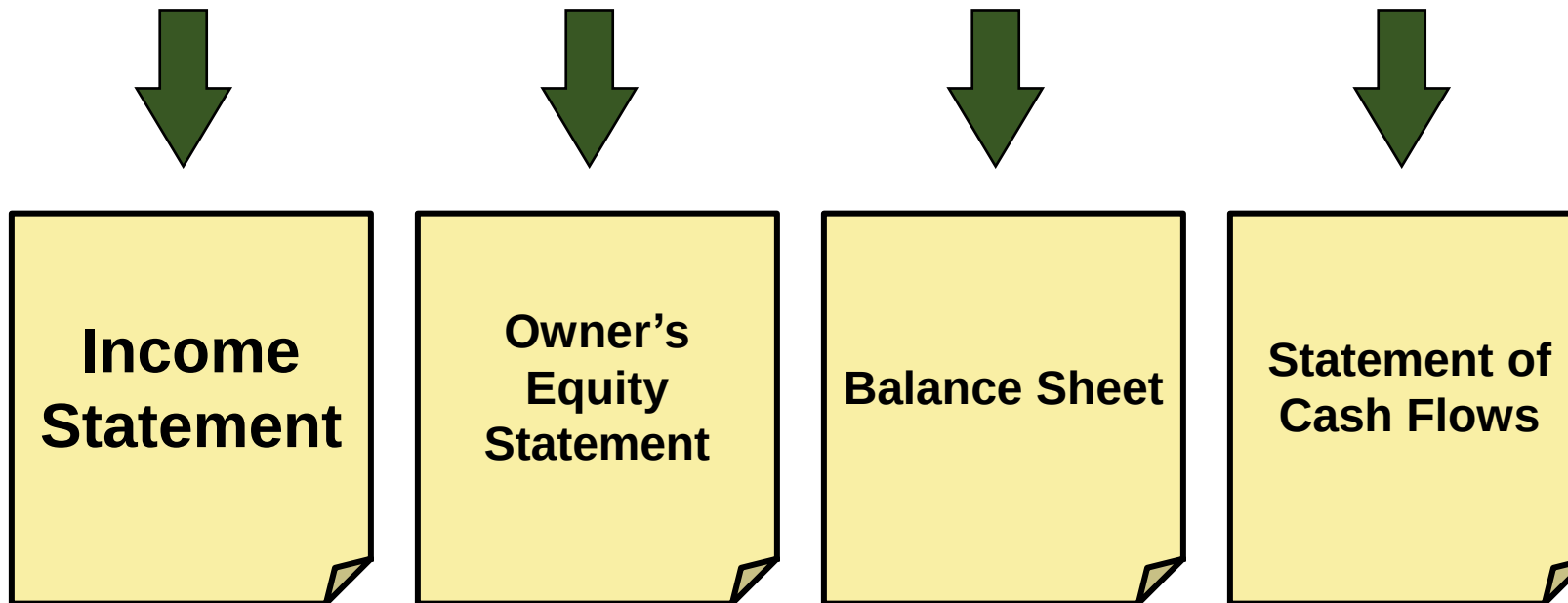
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03

Learning Objectives

- Understand the four financial statements and how they are prepared.
- Identify the sections of a classified balance sheet.
- Explain Types of Companies Based on the Nature of Business. and Ownership.
- Discuss and account for the formation of a partnership.
- Discuss the major characteristics of a corporation.

Describe the four financial statements and how they are prepared.

Companies prepare four financial statements :



Question

Net income will result during a time period when:

- a. assets exceed liabilities.
- b. assets exceed revenues.
- c. expenses exceed revenues.

➔ d. revenues exceed expenses.



SOFTBYTE

Income Statement

For the Month Ended September 30, 2017

Revenues		
Service revenue		\$ 4,700
Expenses		
Salaries and wages expense	\$900	
Rent expense	600	
Advertising expense	250	
Utilities expense	<u>200</u>	
Total expenses		<u>1,950</u>
Net income		<u><u>\$ 2,750</u></u>



SOFTBYTE

Owner's Equity Statement

For the Month Ended September 30, 2017

Owner's capital, September 1		\$ -0-
Add: Investments	\$15,000	
Net income	<u>2,750</u>	<u>17,750</u>
		17,750
Less: Drawings		<u>1,300</u>
Owner's capital, September 30		<u><u>\$16,450</u></u>

SOFTBYTE
 Owner's Equity Statement
 For the Month Ended September 30, 2017

Owner's capital, September 1		\$ -0-
Add: Investments	\$15,000	
Net income	<u>2,750</u>	<u>17,750</u>
		17,750
Less: Drawings		<u>1,300</u>
Owner's capital, September 30		<u>\$16,450</u>

SOFTBYTE
 Balance Sheet
 September 30, 2017

<u>Assets</u>		
Cash		\$ 8,050
Accounts receivable		1,400
Supplies		1,600
Equipment		<u>7,000</u>
Total assets		<u>\$ 18,050</u>
<u>Liabilities and Owner's Equity</u>		
Liabilities		
Accounts payable		\$ 1,600
Owner's equity		
Owner's capital		<u>16,450</u>
Total liabilities and owner's equity		<u>\$ 18,050</u>



SOFTBYTE
Balance Sheet
September 30, 2017

Assets

Cash	\$ 8,050
Accounts receivable	1,400
Supplies	1,600
Equipment	7,000
Total assets	<u>\$ 18,050</u>

Liabilities and Owner's Equity

Liabilities	
Accounts payable	\$ 1,600
Owner's equity	
Owner's capital	<u>16,450</u>
Total liabilities and owner's equity	<u>\$ 18,050</u>



SOFTBYTE
Statement of Cash Flows
For the Month Ended September 30, 2017

Cash flows from operating activities		
Cash receipts from revenues		\$ 3,300
Cash payments for expenses		<u>(1,950)</u>
Net cash provided by operating activities		1,350
Cash flows from investing activities		
Purchase of equipment		(7,000)
Cash flows from financing activities		
Investments by owner	\$15,000	
Drawings by owner	<u>(1,300)</u>	<u>13,700</u>
Net increase in cash		8,050
Cash at the beginning of the period		<u>0</u>
Cash at the end of the period		<u>\$ 8,050</u>

2

3

d

Income Statement

Lecture

- ◆ Reports the revenues and expenses for a specific period of time.
- ◆ Lists revenues first, followed by expenses.
- ◆ Shows net income (or net loss).
- ◆ Does not include investment and withdrawal transactions between the owner and the business in measuring net income.

Owner's Equity Statement

Lecture

- ◆ Reports the changes in owner's equity for a specific period of time.
- ◆ The time period is the same as that covered by the income statement.

Balance Sheet

Lecture

- ◆ Reports the assets, liabilities, and owner's equity at a specific date.
- ◆ Lists assets at the top, followed by liabilities and owner's equity.
- ◆ Total assets must equal total liabilities and owner's equity.
- ◆ Is a snapshot of the company's financial condition at a specific moment in time (usually the month-end or year-end).

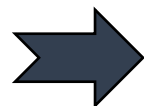
Statement of Cash Flows

Lecture

- ◆ Information on the cash receipts and payments for a specific period of time.
- ◆ Answers the following:
 - ▶ Where did cash come from?
 - ▶ What was cash used for?
 - ▶ What was the change in the cash balance?

Question

Which of the following financial statements is prepared as of a specific date?

- 
- a. Balance sheet.
 - b. Income statement.
 - c. Owner's equity statement.
 - d. Statement of cash flows.

Financial Statements

Lecture

Presented below is selected information related to Flanagan Company at December 31, 2017. Flanagan reports financial information monthly.

Equipment	\$10,000	Utilities Expense	\$ 4,000
Cash	8,000	Accounts Receivable	9,000
Service Revenue	36,000	Salaries and Wages Expense	7,000
Rent Expense	11,000	Notes Payable	16,500
Accounts Payable	2,000	Owner's Drawings	5,000

- (a) Determine the total assets of at December 31, 2017.
- (b) Determine the net income reported for December 2017.
- (c) Determine the owner's equity at December 31, 2017.

Financial Statements

Lecture

Presented below is selected information related to Flanagan Company at December 31, 2017. Flanagan reports financial information monthly.

Equipment	\$10,000	Utilities Expense	\$ 4,000
Cash	8,000	Accounts Receivable	9,000
Service Revenue	36,000	Salaries and Wages Expense	7,000
Rent Expense	11,000	Notes Payable	16,500
Accounts Payable	2,000	Owner's Drawings	5,000

(a) Determine the total assets of at December 31, 2017.

The total assets are \$27,000, comprised of

- Cash \$8,000,
- Accounts Receivable \$9,000, and
- Equipment \$10,000.

Financial Statements

Lecture

Presented below is selected information related to Flanagan Company at December 31, 2017. Flanagan reports financial information monthly.

Equipment	\$10,000	Utilities Expense	\$ 4,000
Cash	8,000	Accounts Receivable	9,000
Service Revenue	36,000	Salaries and Wages Expense	7,000
Rent Expense	11,000	Notes Payable	16,500
Accounts Payable	2,000	Owner's Drawings	5,000

(b) Determine the net income reported for December 2017.

Revenues		
Service revenue		\$36,000
Expenses		
Rent expense	\$11,000	
Salaries and wages expense	7,000	
Utilities expense	<u>4,000</u>	
Total expenses		<u>22,000</u>
Net income		<u><u>\$14,000</u></u>

Financial Statements

Lecture

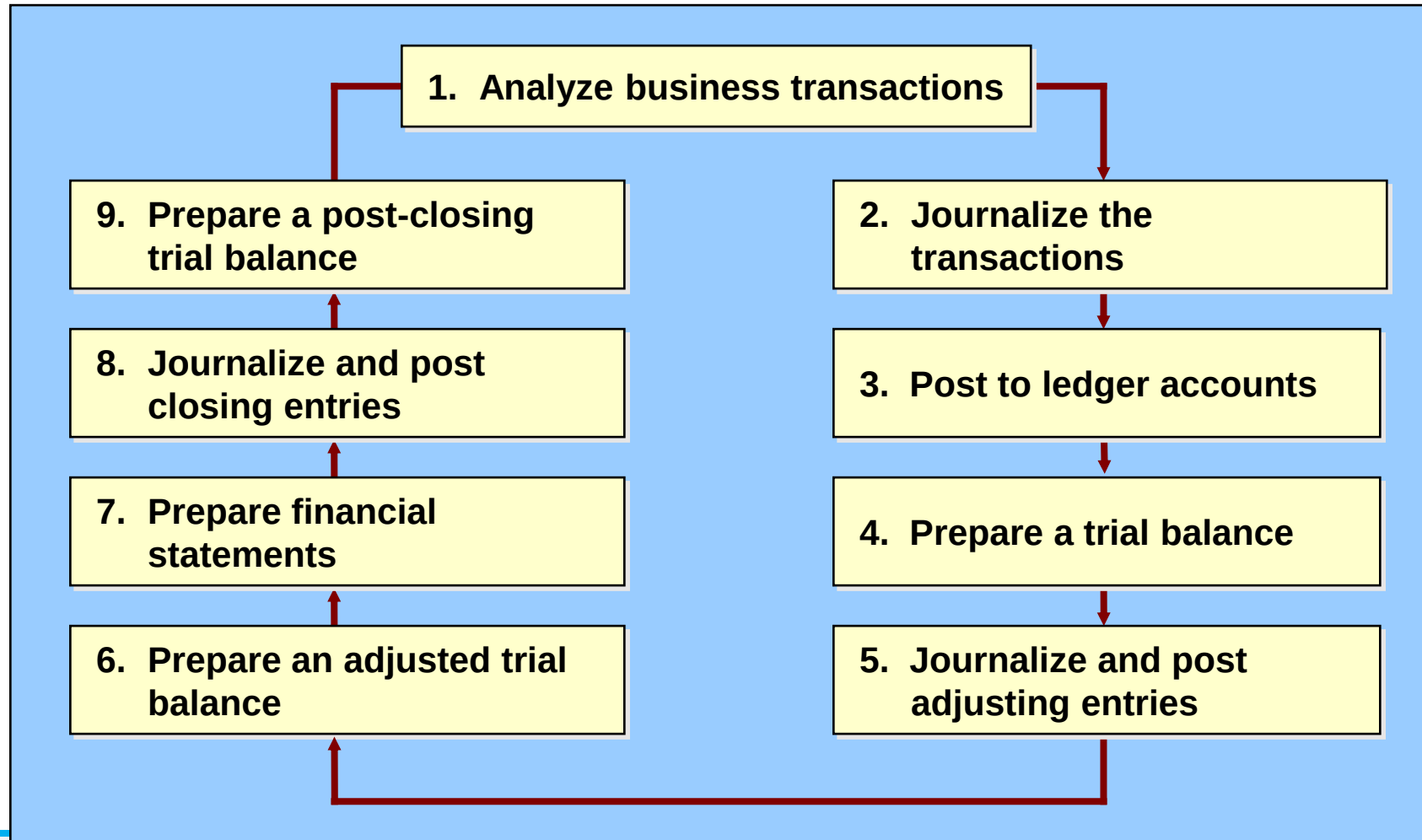
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Equipment	\$10,000	Utilities Expense	\$ 4,000
Cash	8,000	Accounts Receivable	9,000
Service Revenue	36,000	Salaries and Wages Expense	7,000
Rent Expense	11,000	Notes Payable	16,500
Accounts Payable	2,000	Owner's Drawings	5,000

(c) Determine the owner's equity at December 31, 2017.

Total assets [as computed in (a)]		\$27,000
Less: Liabilities		
Notes payable	\$16,500	
Accounts payable	<u>2,000</u>	<u>18,500</u>
Owner's equity		<u><u>\$ 8,500</u></u>

Explain the steps in the accounting cycle and how to prepare correcting entries.



Identify the sections of a classified balance sheet.

Lecture

- ◆ Presents a snapshot at a point in time.
- ◆ To improve understanding, companies group similar assets and similar liabilities together.

Standard Classifications

Assets

Current assets

Long-term investments

Property, plant, and equipment

Intangible assets

Liabilities and Owner's Equity

Current liabilities

Long-term liabilities

Owner's (Stockholders') equity

The Classified Balance Sheet

Lecture

FRANKLIN COMPANY

Balance Sheet

October 31, 2017

Assets

Current assets

Cash		\$ 6,600	
Debt investments		2,000	
Accounts receivable		7,000	
Notes receivable		1,000	
Inventory		3,000	
Supplies		2,100	
Prepaid insurance		400	
Total current assets			\$22,100

Long-term investments

Stock investments		5,200	
Investment in real estate		2,000	7,200

Property, plant, and equipment

Land		10,000	
Equipment	\$24,000		
Less: Accumulated depreciation— equipment	5,000	19,000	29,000

Intangible assets

Patents			3,100
Total assets			\$61,400

The Classified Balance Sheet

Lecture

FRANKLIN COMPANY

Balance Sheet

October 31, 2017

Assets

Current assets

Cash	\$ 6,600	
Debt investments	2,000	
Accounts receivable	7,000	
Notes receivable	1,000	
Inventory	3,000	
Supplies	2,100	
Prepaid insurance	400	
Total current assets		\$22,100

Long-term investments

Stock investments	5,200	
Investment in real estate	2,000	7,200

Property, plant, and equipment

Land		10,000	
Equipment	\$24,000		
Less: Accumulated depreciation— equipment	5,000	19,000	29,000

Intangible assets

Patents			3,100
Total assets			\$61,400

Current Assets

Lecture

- ◆ Assets that a company expects to **convert to cash** or **use up** within one year or the operating cycle, whichever is longer.
- ◆ **Operating cycle** is the average time that it takes to purchase inventory, sell it on account, and then collect cash from customers.

Current Assets

Lecture

SOUTHWEST AIRLINES CO.

Balance Sheet (partial)
(in millions)

Current assets

Cash and cash equivalents	\$1,390
Short-term investments	369
Accounts receivable	241
Inventories	181
Prepaid expenses and other current assets	420
Total current assets	<u>\$2,601</u>

Usually listed in the order they expect to convert them into cash.

Question

The correct order of presentation in a classified balance sheet for the following current assets is:

- a. accounts receivable, cash, prepaid insurance, inventory.
- b. cash, inventory, accounts receivable, prepaid insurance.
- ➔ c. cash, accounts receivable, inventory, prepaid insurance.
- d. inventory, cash, accounts receivable, prepaid insurance

Long-Term Investments

Lecture

- ◆ Investments in stocks and bonds of other companies.
- ◆ Investments in long-term assets such as land or buildings that is not currently being used in operating activities.
- ◆ Long-term notes receivable.

YAHOO! INC. Balance Sheet (partial) (in thousands)	
Long-term investments	
Investments in securities	\$90,266

Property, Plant, and Equipment

Lecture

- ◆ Long useful lives.
- ◆ Currently used in operations.
- ◆ **Depreciation** - allocating the cost of assets to a number of years.
- ◆ **Accumulated depreciation** - total amount of depreciation expensed thus far in the asset's life.

Property, Plant, and Equipment

Lecture

COOPER TIRE & RUBBER COMPANY

Balance Sheet (partial)
(in thousands)

Property, plant, and equipment

Land and land improvements	\$ 41,553	
Buildings	298,706	
Machinery and equipment	1,636,091	
Molds, cores, and rings	<u>268,158</u>	\$2,244,508
Less: Accumulated depreciation		<u>1,252,692</u>
		\$ 991,816

Intangible Assets

Lecture

- ◆ Long-lived assets that do not have physical substance.

TIME WARNER, INC. Balance Sheet (partial) (in millions)	
Intangible assets	
Goodwill	\$40,953
Film library	2,690
Customer lists	2,540
Cable television franchises	38,048
Sports franchises	262
Brands, trademarks, and other intangible assets	8,313
	\$92,806

The Classified Balance Sheet

Lecture

Question

Patents and copyrights are

- a. Current assets.
- ➔ b. Intangible assets.
- c. Long-term investments.
- d. Property, plant, and equipment.

Current Liabilities

Lecture

MARCUS CORPORATION

Balance Sheet (partial)
(in thousands)

Current liabilities

Notes payable	\$ 239
Accounts payable	24,242
Current maturities of long-term debt	57,250
Other current liabilities	27,477
Income taxes payable	11,215
Salaries and wages payable	6,720
Total current liabilities	<u>\$127,143</u>

Long-Term Liabilities

Lecture

- ◆ Obligations a company expects to pay **after** one year.

THE PROCTER & GAMBLE COMPANY	
Balance Sheet (partial)	
(in millions)	
Long-term liabilities	
Long-term debt	\$23,375
Deferred income taxes	12,015
Other noncurrent liabilities	<u>5,147</u>
Total long-term liabilities	\$40,537

Question

Which of the following is not a long-term liability?

- a. Bonds payable
- ➔ b. Current maturities of long-term obligations
- c. Long-term notes payable
- d. Mortgages payable

Owner's Equity

Lecture

- ◆ Proprietorship - one capital account.
- ◆ Partnership - capital account for each partner.
- ◆ Corporation - Common Stock and Retained Earnings.

Real World		NORDSTROM, INC. Balance Sheet (partial) (\$ in thousands)	
Stockholders' equity			
Common stock, 271,331 shares			\$ 685,934
Retained earnings			<u>1,406,747</u>
Total stockholders' equity			\$2,092,681

Financial Statements

Lecture

The following accounts were taken from the financial statements of Callahan Company.

Salaries and wages payable

Service revenue

Interest payable

Goodwill

Debt investments (short-term)

Mortgage payable (due
in 3 years)

Stock investments (long-term)

Equipment

Accumulated depreciation—
equipment

Depreciation expense

Owner's capital

Unearned service revenue

Match each of the following accounts to its proper balance sheet classification, shown below. If the item would not appear on a balance sheet, use “NA.”

Current assets (CA)

Long-term investments (LTI)

Property, plant, and equipment (PPE)

Intangible assets (IA)

Current liabilities (CL)

Long-term liabilities (LTL)

Owner's equity (OE)

The formation of a partnership.

Lecture

Partnership, an association of two or more persons to carry on as co-owners of a business for profit.

Type of Business:

- ◆ Small retail, service, or manufacturing companies.
- ◆ Accountants, lawyers, and doctors.

Characteristics of Partnerships

Lecture

ASSOCIATION OF INDIVIDUALS

- ◆ Legal entity.
- ◆ Accounting entity.
- ◆ Net income not taxed as a separate entity.

MUTUAL AGENCY

- ◆ Act of any partner is binding on all other partners, so long as the act appears to be appropriate for the partnership.

Characteristics of Partnerships

Lecture

LIMITED LIFE

- ◆ Dissolution occurs whenever a partner withdraws or a new partner is admitted.
- ◆ Dissolution does not mean the business ends.

UNLIMITED LIABILITY

- ◆ Each partner is personally and individually liable for all partnership liabilities.

CO-OWNERSHIP OF PROPERTY

- ◆ Each partner has a claim on total assets.
- ◆ This claim does not attach to specific assets.
- ◆ All net income or net loss is shared equally by the partners, unless otherwise stated in the partnership agreement.

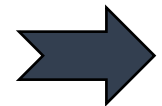
Characteristics of Partnerships

Lecture

Question

All of the following are characteristics of partnerships except:

- a. co-ownership of property.
- b. mutual agency.
- c. limited life.



- d. limited liability.

Characteristics of a corporation.

Lecture

An entity separate and distinct from its owners.

Classified by Purpose

- ◆ Not-for-Profit
- ◆ For Profit

- ▶ Salvation Army
- ▶ American Cancer Society

Classified by Ownership

- ◆ Publicly held
- ◆ Privately held

- ▶ McDonald's
- ▶ Nike
- ▶ PepsiCo
- ▶ Google
- ▶ Cargill Inc.

Characteristics of a corporation.

Lecture

Characteristics that distinguish corporations from proprietorships and partnerships.

- ◆ Separate Legal Existence
- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital
- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes

Advantages

Disadvantages

Characteristics of a corporation.

Lecture

Characteristics that distinguish corporations from proprietorships and partnerships.

- ◆ Separate Legal Existence →
- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital
- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes

Corporation acts under its own name rather than in the name of its stockholders.

Characteristics of a corporation.

Lecture

Characteristics that distinguish corporations from proprietorships and partnerships.

- ◆ Separate Legal Existence
- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital
- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes

→ Limited to their investment.

Characteristics of a corporation.

Lecture

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- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes

Shareholders may sell their stock.

Characteristics of Partnerships

Lecture

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- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital →
- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes

Corporation can obtain capital through the issuance of stock.

Characteristics of Partnerships

Characteristics that distinguish corporations from proprietorships and partnerships.

- ◆ Separate Legal Existence
- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital
- ◆ Continuous Life →
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes

Continuance as a going concern is not affected by the withdrawal, death, or incapacity of a stockholder, employee, or officer.

Financial Statements

Lecture

Characteristics that distinguish corporations from proprietorships and partnerships.

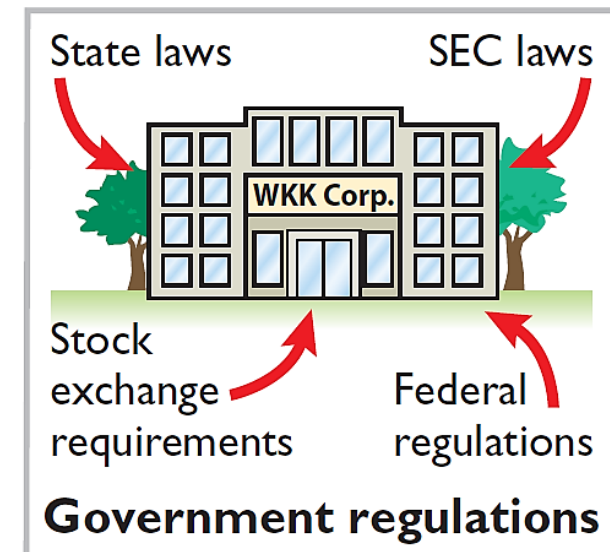
- ◆ Separate Legal Existence
- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital
- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes

Separation of ownership and management often reduces an owner's ability to actively manage the company.

Characteristics of a Corporation

Characteristics that distinguish corporations from proprietorships and partnerships.

- ◆ Separate Legal Existence
- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital
- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes



Financial Statements

Lecture

Characteristics that distinguish corporations from proprietorships and partnerships.

- ◆ Separate Legal Existence
- ◆ Limited Liability of Stockholders
- ◆ Transferable Ownership Rights
- ◆ Ability to Acquire Capital
- ◆ Continuous Life
- ◆ Corporate Management
- ◆ Government Regulations
- ◆ Additional Taxes



Corporations pay income taxes as a separate legal entity and in addition, stockholders pay taxes on cash dividends.

Business Sectors

Lecture

👉 Service-sector companies



👉 Merchandising-sector companies



👉 Manufacturing-sector companies



Financial Statements

Lecture



Financial Statements

Lecture

The Parts Shoppe

Balance Sheet

May 31, 20~

Assets

Current Assets

Bank		\$ 47,751	
Accounts Receivable	\$ 23,829		
Allowance for Doubtful Accounts	<u>(390)</u>	23,439	
Merchandise Inventory		54,970	
Supplies		8,840	
Prepaid Insurance		7,792	
Prepaid Rent		<u>3,758</u>	
Total Current Assets			\$ 146,551

Financial Statements

Lecture

CALIFORNIA BUSINESS SOLUTIONS Simple Income Statement For Year Ended December 31, 2018

Revenues		
Net sales		\$293,500
Interest Revenue		<u>5,650</u>
Total Revenues		299,150
Expenses		
Cost of Goods Sold	\$180,000	
Total Selling Expenses	46,250	
Total General and Administrative Expenses	12,800	
Interest Expense	<u>8,400</u>	
Total Expenses		<u>247,450</u>
Net Income		<u>\$ 51,700</u>

CALIFORNIA BUSINESS SOLUTIONS
Simple Income Statement
For Year Ended December 31, 2018

Revenues

Net sales \$293,500

Interest Revenue 5,650

Total Revenues 299,150

Expenses

Cost of Goods Sold \$180,000

Total Selling Expenses 46,250

Total General and Administrative Expenses 12,800

Interest Expense 8,400

Total Expenses 247,450

Net Income \$ 51,700



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