

Principles of Accounting

MGM 227

**Prepared by
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Completing the Accounting Cycle

Lecture 10



Changes in the Accounting Equation/Debits and Credits

Assets = Liabilities + Equity


Debits = Credits

WHICH BECOMES:

Assets + Expenses + Drawings = Liabilities + (Capital contributions + Income)


All Debits = All Credits

Ledger Account

Three basic parts

- title
- place for recording increases
- place for recording decreases

Account Title					
Date	Explanation	Amount	Date	Explanation	Amount
← Debit (Dr) side →			← Credit (Cr) side →		

- **General Journal**

• <u>Date</u>	<u>Details</u>	<u>Debit (\$)</u>	<u>Credit (\$)</u>
• 2 July	Cash at Bank	120 000	
•	Nicole Andreou, Capital		120 000
-----**Cash invested by the owner-----			
• 2 July	Rent expense	1 800	
•	Cash at Bank		1 800
-----**Rent paid -----			
• 3 July	Equipment	70 000	
•	Cash at Bank		32 000
	Loan payable		38 000
-----**Equipment purchased for cash and loan payable-----			

• 4 July	Supplies	8 400	
	Cash at Bank		8 400
-----**Supplies purchased-----			
• 6 July	Advertising expense	890	
	Cash at Bank		890
-----**Cash paid for advertising -----			
• 16 July	Cash at Bank	3250	
	Accounts Receivable	620	
	Revenue		3 870
-----**Revenue for first half of month-----			

• 31 July	Cash at Bank	3 680	
	Accounts Receivable	580	
		Revenue	4 260
-----**Revenue for second part of the month-----			
• 31 July	Telephone expense	330	
		Cash at Bank	330
-----**Telephone expenses paid -----			

Cash at Bank - 100

2/07	Nicole Andreou – Capital	120 000	2/07	Rent expense	1 800
			3/07	Equipment	32 000
			4/07	Supplies	8 400
			6/07	Advertising expense	890
16/07	Revenue	3 250	20/07	Insurance expense	480
	Accounts Receivable		28/07	Nicole Andreou – Drawings	560
23/07		140	31/07	Telephone expenses	330
31/07	Revenue	3 680		Bal c/f	<u>82 610</u>
		<u>.</u>			127 070
		127 070			
	Bal b/d	82 610			

Accounts Receivable					
16/07	Revenue	\$620	23/07	Cash	\$140
31/07	Revenue	580		Bal c/f	1 060
		<u>1 200</u>			<u>1 200</u>
	Bal c/d	1 060			
Supplies – 102					
4/07	Cash at Bank	\$8 400			
Equipment – 103					
3/7	Cash and loan payable	\$70 000			
Loan payable – 200					
			3/7	Equipment	38 000

• **Nicole Andreou, Capital – 300**

		2/7	Cash at Bank	
			120 000	

Nicole Andreou, Drawings - 301

28/7	Cash at Bank	\$560	
------	--------------	-------	--

Revenue – 400

		16/7	Cash & Accounts receivable	\$3 870
	Bal c/f	8 130	31/07	Cash & Accounts receivable
				4 260
		<u>8 130</u>		<u>8 130</u>
			Bal c/d	8 130

Rent expense – 500

2/7	Cash at Bank	1 800
-----	--------------	-------

Advertising expense – 501

6/7	Cash at Bank	890
-----	--------------	-----

Insurance expense

20/7	Cash at Bank	480
------	--------------	-----

Telephone expense

31/07	Cash at Bank	330
-------	--------------	-----

NICOLE ANDREOU BEAUTY SALON
Trial Balance
as at 31 July 2018

Account	Account No.	Debit	Credit
Cash at Bank	100	\$82 610	
Accounts Receivable	101	1 060	
Supplies	102	8 400	
Equipment	103	70 p00	
Loan Payable	200		\$38 000
Nicole Andreou, Capital	300		120 000
Nicole Andreou, Drawings	301	560	
Revenue	400		8 130
Rent Expense	500	1 800	
Advertising Expense	501	890	
Insurance Expense	502	480	
Telephone Expense	503	330	
		<u>\$166 130</u>	<u>\$166 130</u>

d) Preparation of Financial statements

NICOLE ANDREOU BEAUTY SALON
Income Statement
For the month ended 31 July 2018

INCOME

Revenue \$8 130

EXPENSES

Rent expense \$1 800

Advertising expense 890

Insurance expense 480

Telephone expense 330

3 500

PROFIT

\$4 630

NICOLE ANDREOU BEAUTY SALON
Statement of Changes in Equity
For the month ended 31 July 2018

N. Andreou, Capital – 1 July 2018	\$0
Add: Capital contribution	120 000
Profit	4 630
	124 630
Less: Drawings	560
N. Andreou, Capital – 31 July 2018	\$124 070

NICOLE ANDREOU BEAUTY SALON
Balance Sheet
As at 31 July 2018

ASSETS

Cash at bank	\$82 610
Accounts Receivable	1 060
Supplies	8 400
Equipment	70 000
TOTAL ASSETS	\$162 070

LIABILITIES

Loan payable	38 000
TOTAL LIABILITIES	38 000
NET ASSETS	\$124 070

EQUITY

N. Andreou, Capital	\$124 070
TOTAL EQUITY	\$124 070

Using A Worksheet

Worksheet

- A multiple-column form used in preparing financial statements.
- Not a permanent accounting record.
- Five step process.
- Use of worksheet is optional.

Steps in Preparing a Worksheet

Illustration 4

Worksheet.xls

File Edit View Insert Format Tools Data Window Help

	A	B	C	D	E	F	G	H	I	J	K
1		Worksheet									
2		Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
3											
4	Account Titles	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
5											
6											
7											
8											
9											
10											
11											
12											
13											
14											
15											

1

Prepare a trial balance on the worksheet

2

Enter adjustment data

3

Enter adjusted balances

4

Extend adjusted balances to appropriate statement columns

5

Total the statement columns, compute net income (or net loss), and complete worksheet

Steps in Preparing a Worksheet

Illustration:

Illustration 4-2
Preparing a trial balance

PIONEER ADVERTISING AGENCY INC. Worksheet For the Month Ended October 31, 2011										
Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200									
Advertising Supplies	2,500									
Prepaid Insurance	600									
Office Equipment	5,000									
Notes Payable		5,000								
Accounts Payable		2,500								
Unearned Revenue		1,200								
Share Capital		10,000								
Dividends	500									
Service Revenue		10,000								
Salaries Expense	4,000									
Rent Expense	900									
Totals	28,700	28,700								

Steps in Preparing a Worksheet

1. Prepare a Trial Balance on the Worksheet

Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200									
Advertising Supplies	2,500									
Prepaid Insurance	600									
Office Equipment	5,000									
Notes Payable		5,000								
Accounts Payable		2,500								
Unearned Revenue		1,200								
Share Capital		10,000								
Dividends	500									
Service Revenue		10,000								
Salaries Expense	4,000									
Rent	900									
Totals	28,700	28,700								

Include all accounts with balances.

Trial balance amounts come directly from ledger accounts.

Steps in Preparing a Worksheet

Illustration 3-22

General journal
showing adjusting
entries

Adjusting Journal Entries

2011

GENERAL JOURNAL					J2
Date	Account Titles and Explanation	Ref.	Debit	Credit	
2010	<u>Adjusting Entries</u>				
Oct. 31	Advertising Supplies Expense	631	1,500		
	Advertising Supplies	126		1,500	
	(To record supplies used)				
31	Insurance Expense	722	50		
	Prepaid Insurance	130		50	
	(To record insurance expired)				
31	Depreciation Expense	711	40		
	Accumulated Depreciation—Office Equipment	158		40	
	(To record monthly depreciation)				
31	Unearned Revenue	209	400		
	Service Revenue	400		400	
	(To record revenue for services provided)				
31	Accounts Receivable	112	200		
	Service Revenue	400		200	
	(To record revenue for services provided)				
31	Interest Expense	905	50		
	Interest Payable	230		50	
	(To record interest on notes payable)				
31	Salaries Expense	726	1,200		
	Salaries Payable	212		1,200	
	(To record accrued salaries)				

Steps in Preparing a Worksheet

2. Enter the Adjustments in the Adjustments Columns

Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200									
Advertising Supplies	2,500		(a) 1,500							
Prepaid Insurance	600		(b) 50							
Office Equipment	5,000									
Notes Payable		5,000								
Accounts Payable		2,500								
Unearned Revenue		1,200	(d) 400							
Share Capital		10,000								
Dividends	500									
Service Revenue		10,000	(d) 400							
			(e) 200							
Salaries Expense	4,000		(g) 1,200							
Rent	900									
Totals	28,700	28,700								
Advertising Supplies Expense			(a) 1,500							
Insurance Expense			(b) 50							
Accumulated Depreciation			(c) 40							
Depreciation Expense			(c) 40							
Accounts Receivable			(e) 200							
Interest Expense			(f) 50							
Interest Payable			(f) 50							
Salaries Payable			(g) 1,200							
Totals			3,440	3,440						

Adjustments Key:

- (a) Supplies Used.
- (b) Insurance Expired.
- (c) Depreciation Expensed.
- (d) Service Revenue Earned.
- (e) Service Revenue Accrued.
- (f) Interest Accrued.
- (g) Salaries Accrued.

Enter adjustment amounts, total adjustments columns, and check for equality.

Add additional accounts as needed.

Steps in Preparing a Worksheet

3. Complete the Adjusted Trial Balance Columns

Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200				15,200					
Advertising Supplies	2,500			(a) 1,500	1,000					
Prepaid Insurance	600			(b) 50	550					
Office Equipment	5,000				5,000					
Notes Payable		5,000				5,000				
Accounts Payable		2,500				2,500				
Unearned Revenue		1,200	(d) 400			800				
Share Capital		10,000				10,000				
Dividends	500				500					
Service Revenue		10,000		(d) 400 (e) 200		10,600				
Salaries Expense	4,000		(g) 1,200		5,200					
Rent	900				900					
Totals	28,700	28,700								
Advertising Supplies Expense			(a) 1,500		1,500					
Insurance Expense			(b) 50		50					
Accumulated Depreciation				(c) 40		40				
Depreciation Expense			(c) 40		40					
Accounts Receivable			(e) 200		200					
Interest Expense			(f) 50		50					
Interest Payable				(f) 50		50				
Salaries Payable				(g) 1,200		1,200				
Totals			3,440	3,440	30,190	30,190				

Total the adjusted trial balance columns and check for equality.

Steps in Preparing a Worksheet

4. Extend Amounts to Financial Statement Columns

Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200				15,200					
Advertising Supplies	2,500			(a) 1,500	1,000					
Prepaid Insurance	600			(b) 50	550					
Office Equipment	5,000				5,000					
Notes Payable		5,000				5,000				
Accounts Payable		2,500				2,500				
Unearned Revenue		1,200	(d) 400			800				
Share Capital		10,000				10,000				
Dividends	500				500					
Service Revenue		10,000		(d) 400 (e) 200		10,600		10,600		
Salaries Expense	4,000		(g) 1,200		5,200		5,200			
Rent	900				900		900			
Totals	28,700	28,700								
Advertising Supplies Expense			(a) 1,500		1,500		1,500			
Insurance Expense			(b) 50		50		50			
Accumulated Depreciation				(c) 40		40				
Depreciation Expense			(c) 40		40		40			
Accounts Receivable			(e) 200		200					
Interest Expense			(f) 50		50		50			
Interest Payable				(f) 50		50				
Salaries Payable				(g) 1,200		1,200				
Totals			3,440	3,440	30,190	30,190	7,740	10,600		

Extend all revenue and expense account balances to the income statement columns.

Steps in Preparing a Worksheet

4. Extend Amounts to Financial Statement Columns

Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200				15,200				15,200	
Advertising Supplies	2,500			(a) 1,500	1,000				1,000	
Prepaid Insurance	600			(b) 50	550				550	
Office Equipment	5,000				5,000				5,000	
Notes Payable		5,000				5,000				5,000
Accounts Payable		2,500				2,500				2,500
Unearned Revenue		1,200	(d) 400			800				800
Share Capital		10,000				10,000				10,000
Dividends	500				500				500	
Service Revenue		10,000		(d) 400 (e) 200		10,600	10,600			
Salaries Expense	4,000		(g) 1,200		5,200		5,200			
Rent	900				900		900			
Totals	28,700	28,700								
Advertising Supplies Expense			(a) 1,500		1,500		1,500			
Insurance Expense			(b) 50		50		50			
Accumulated Depreciation				(c) 40		40				40
Depreciation Expense			(c) 40		40		40			
Accounts Receivable			(e) 200		200				200	
Interest Expense			(f) 50		50		50			
Interest Payable				(f) 50		50				50
Salaries Payable				(g) 1,200		1,200				1,200
Totals			3,440	3,440	30,190	30,190	7,740	10,600	22,450	19,590

Extend all asset, liability, and equity account balances to the statement of financial position columns.

Steps in Preparing a Worksheet

5. Total Columns, Compute Net Income (Loss)

Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200				15,200				15,200	
Advertising Supplies	2,500			(a) 1,500	1,000				1,000	
Prepaid Insurance	600			(b) 50	550				550	
Office Equipment	5,000				5,000				5,000	
Notes Payable		5,000				5,000				5,000
Accounts Payable		2,500				2,500				2,500
Unearned Revenue		1,200	(d) 400			800				800
Share Capital		10,000				10,000				10,000
Dividends	500				500				500	
Service Revenue		10,000		(d) 400 (e) 200		10,600		10,600		
Salaries Expense	4,000		(g) 1,200		5,200		5,200			
Rent	900				900		900			
Totals	28,700	28,700								
Advertising Supplies Expense			(a) 1,500		1,500		1,500			
Insurance Expense			(b) 50		50		50			
Accumulated Depreciation				(c) 40		40				40
Depreciation Expense			(c) 40		40		40			
Accounts Receivable			(e) 200		200				200	
Interest Expense			(f) 50		50		50			
Interest Payable				(f) 50		50				50
Salaries Payable				(g) 1,200		1,200				1,200
Totals			3,440	3,440	30,190	30,190	7,740	10,600	22,450	19,590
Net income							2,860			2,860
Totals							10,600	10,600	22,450	22,450

Compute Net Income or Net Loss.

Preparing Adjusting Entries from a Worksheet

Adjusting Entries



- The adjusting entries are prepared from the adjustments columns of the worksheet.
- Journalizing and posting of adjusting entries follows the preparation of financial statements when a worksheet is used.

Closing the Books

At the end of the accounting period, the company makes the accounts ready for the next period.

Illustration 4-5

TEMPORARY

These accounts are closed

All revenue accounts

All expense accounts

Dividends

PERMANENT

These accounts are not closed

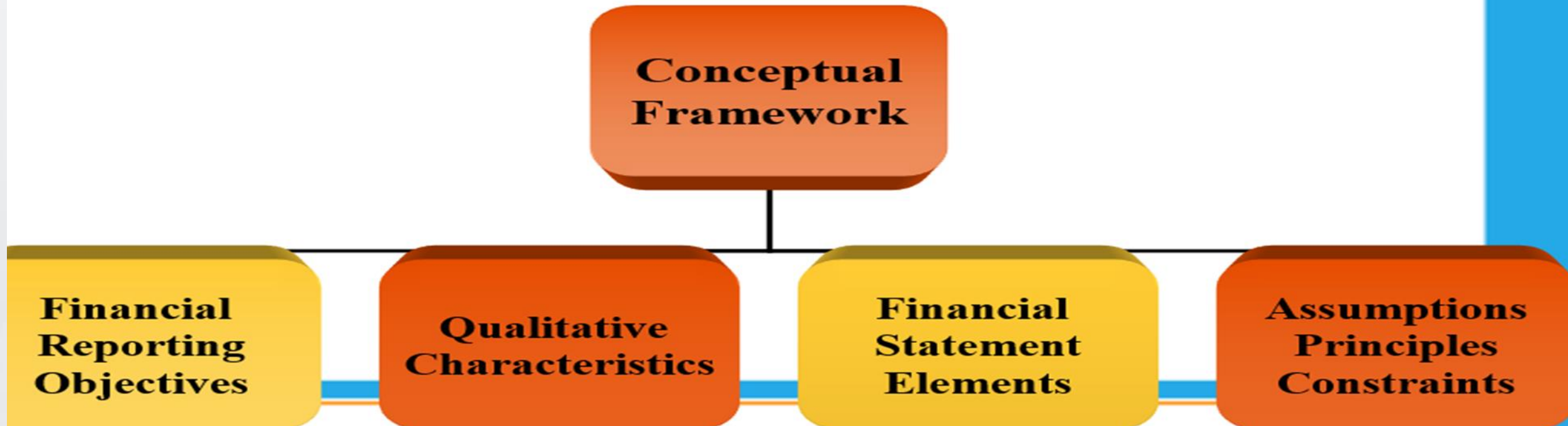
All asset accounts

All liability accounts

Equity

GAAP & CONCEPTUAL FRAMEWORK

The FASB developed a
CONCEPTUAL FRAMEWORK
to resolve accounting and reporting problems.



QUALITATIVE CHARACTERISTICS

Useful information is:

RELEVANT

RELIABLE

COMPARABLE

CONSISTENT

RELEVANCE

RELEVANT INFORMATION:

- **Makes a difference in a decision.**
- **Has predictive value and feedback value.**
- **Is timely.**

RELIABILITY

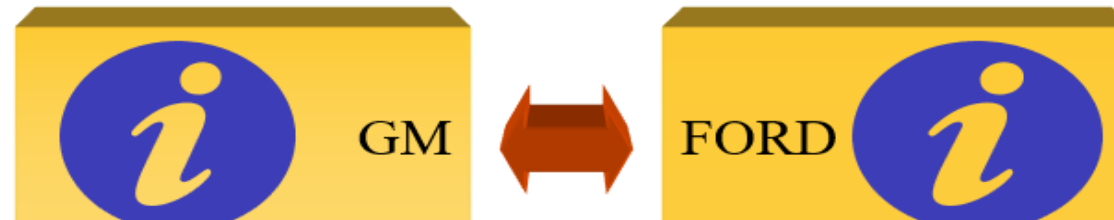
RELIABLE INFORMATION

- Is dependable and verifiable.
- Is free of error and bias.
- Is a faithful representation.
- Is factual.

COMPARABILITY

COMPARABLE INFORMATION

- Accounting information from two similar companies should be comparable.
- Different companies in similar industries should use the same accounting principles.



CONSISTENCY

CONSISTENT INFORMATION

- Companies should use the same accounting principles from year to year.
- Changes in accounting principles must be justifiable.



BASIC ACCOUNTING ASSUMPTIONS

Monetary unit

Economic entity

Time period

Going concern

MONETARY UNIT ASSUMPTION

Only transaction data that can be expressed in terms of money be included in the accounting records.



ECONOMIC ENTITY ASSUMPTION

The activities of the entity are to be kept separate and distinct from the activities of the owner and all other economic entities.



BMW

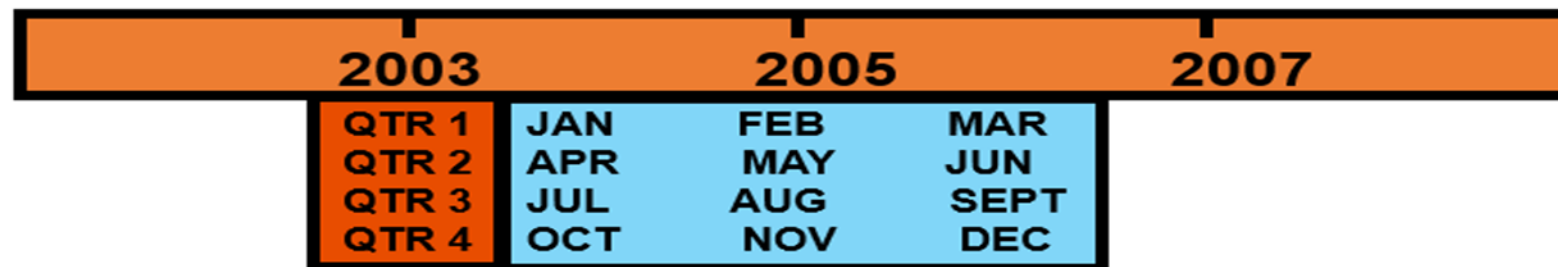


Benz

Economic events can be identified with a particular unit of accountability

TIME PERIOD ASSUMPTION

The economic life of a business can be divided into artificial time periods



GOING CONCERN ASSUMPTION

The enterprise will continue in operation long enough to carry out its existing objectives.



NOW



FUTURE

BASIC ACCOUNTING PRINCIPLES

- 1. REVENUE RECOGNITION**
- 2. MATCHING**
- 3. FULL DISCLOSURE**
- 4. COST**

Assets – Liabilities = Stockholders' Equity

REVENUE RECOGNITION PRINCIPLE

Revenue should be recognized in the accounting period in which it is earned.

When a sale is involved, revenue is recognized at the point of sale.

MATCHING PRINCIPLE

**Expenses are matched with revenues
in the period in which efforts
are made to generate revenues.**

Types of costs

Expired Costs

**Generate revenues
only in the current
accounting period.**

Unexpired Costs

**Generate revenues
in future accounting
periods.**

EXPENSE RECOGNITION PATTERN

Operating expenses contribute to the revenues of the period but their association with revenues is less direct than for cost of goods sold.



FULL DISCLOSURE PRINCIPLE

Requires that circumstances and events that make a difference to financial statement users are to be disclosed in one of two places

Body/Data

Notes

**SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES USUALLY
THE FIRST FOOTNOTE**

COST PRINCIPLE

Requires assets to be recorded at cost.

COST

is relevant because it represents:

**PRICE PAID
or
ASSETS SACRIFICED
or
COMMITMENT MADE**

COST

is reliable because it is:

**OBJECTIVELY
MEASURABLE
and
FACTUAL
and
VERIFIABLE**

BASIC ACCOUNTING CONSTRAINTS

Study Objective 6

Materiality



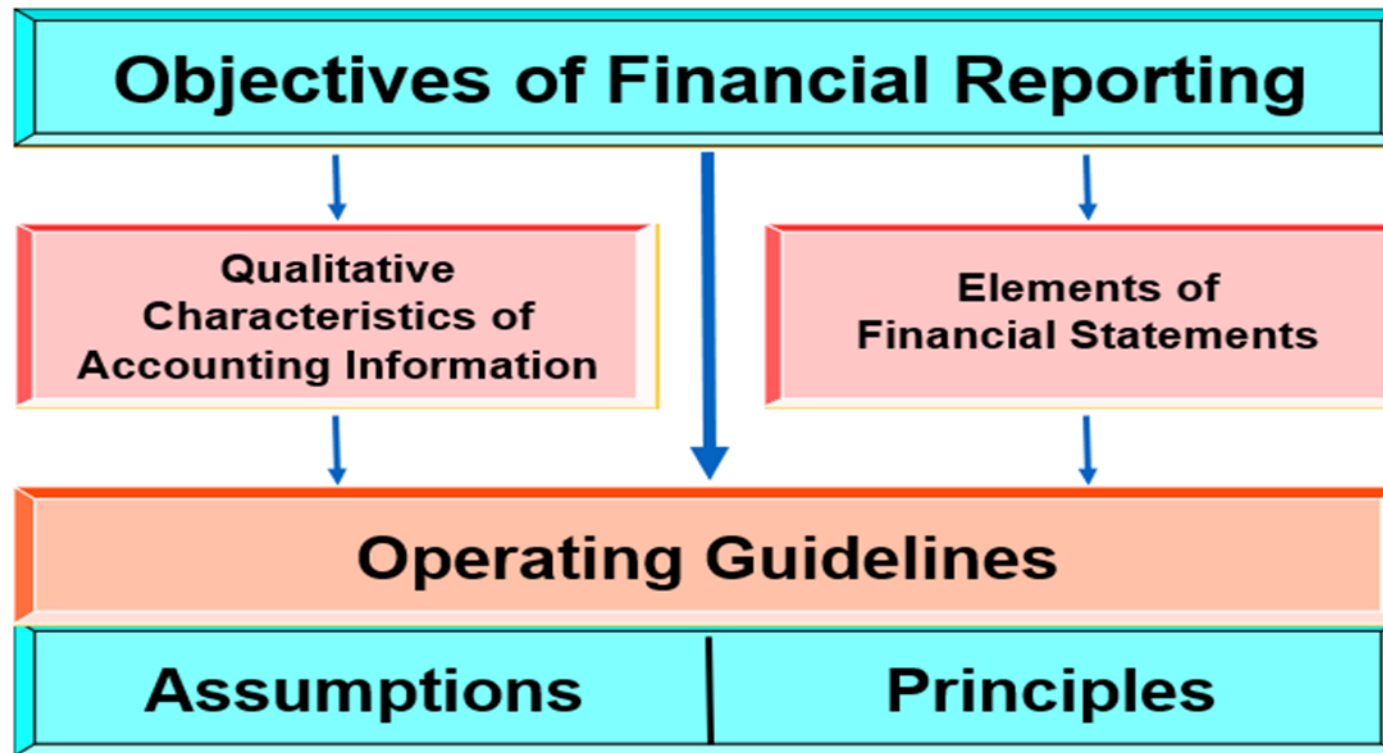
For small amounts, GAAP does not have to be followed.

Conservatism



When in doubt, choose the solution that will be least likely to overstate assets and income.

SUMMARY OF CONCEPTUAL FRAMEWORK





Thank You