



مجموعة جامعة
الجميع الذكية
للتعليم القابضة

MIDOCEAN
UNIVERSITY
BY EVERYONE'S SMART UNIVERSITY

Training Course Fundamentals of Accounting for Non-Professionals

Lecture 2

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Learning Objectives

- **State the basic accounting equation, and define its components.**
- **State the Expanded Accounting Equation and define its components.**
- **Analyze the effects of business transactions on the accounting equation.**
- **Adjusting the errors**

Basic and Expanded Accounting Equations

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



Lecture Outline:

State the accounting equation, and define its components.

Basic Accounting Equation

$$\boxed{\text{Assets}} = \boxed{\text{Liabilities}} + \boxed{\text{Owner's Equity}}$$

State the accounting equation, and define its components.

Basic Accounting Equation

- ◆ Provides the **underlying framework** for recording and summarizing economic events.
- ◆ Assets are claimed by either creditors or owners.
- ◆ If a business is liquidated, claims of creditors must be paid before ownership claims.

State the accounting equation, and define its components.

$$\boxed{\text{Assets}} = \boxed{\text{Liabilities}} + \boxed{\text{Owner's Equity}}$$

Assets

- ◆ Resources a business owns.
- ◆ Provide future services or benefits.
- ◆ Cash, Supplies, Equipment, etc.

State the accounting equation, and define its components.

$$\boxed{\text{Assets}} = \boxed{\text{Liabilities}} + \boxed{\text{Owner's Equity}}$$

Liabilities

- ◆ Claims against assets (debts and obligations).
- ◆ Creditors (party to whom money is owed).
- ◆ Accounts Payable, Notes Payable, Salaries and Wages Payable, etc.

State the accounting equation, and define its components.

$$\boxed{\text{Assets}} = \boxed{\text{Liabilities}} + \boxed{\text{Owner's Equity}}$$

Owner's Equity

- ◆ Ownership claim on total assets.
- ◆ Referred to as residual equity.
- ◆ Investment by owners and revenues (+)
- ◆ Drawings and expenses (-).

State the accounting equation, and define its components.

Owner's Equity

Increases in Owner's Equity

- ◆ **Investments by owner** are the assets the owner puts into the business.
- ◆ **Revenues** result from business activities entered into for the purpose of earning income.
 - ▶ **Common sources of revenue** are: sales, fees, services, commissions, interest, dividends, royalties, and rent.

State the accounting equation, and define its components.

Owner's Equity

Decreases in Owner's Equity

- ◆ **Drawings** An owner may withdraw cash or other assets for personal use.
- ◆ **Expenses** are the cost of assets consumed or services used in the process of earning revenue.
 - ▶ **Common expenses** are: salaries expense, rent expense, utilities expense, tax expense, etc.

State the accounting equation, and define its components.

Expanded accounting equation

Basic Equation	Assets = Liabilities + Owner's Equity
Expanded Equation	Assets = Liabilities + Owner's Capital - Owner's Drawings + Revenues - Expenses

State the accounting equation, and define its components.

Classify the following items as investment by owner, owner's drawings, revenue, or expenses. Then indicate whether each item increases or decreases owner's equity.

	<u>Classification</u>	<u>Effect on Equity</u>
1. Rent Expense		
2. Service Revenue		

Expense

Decrease

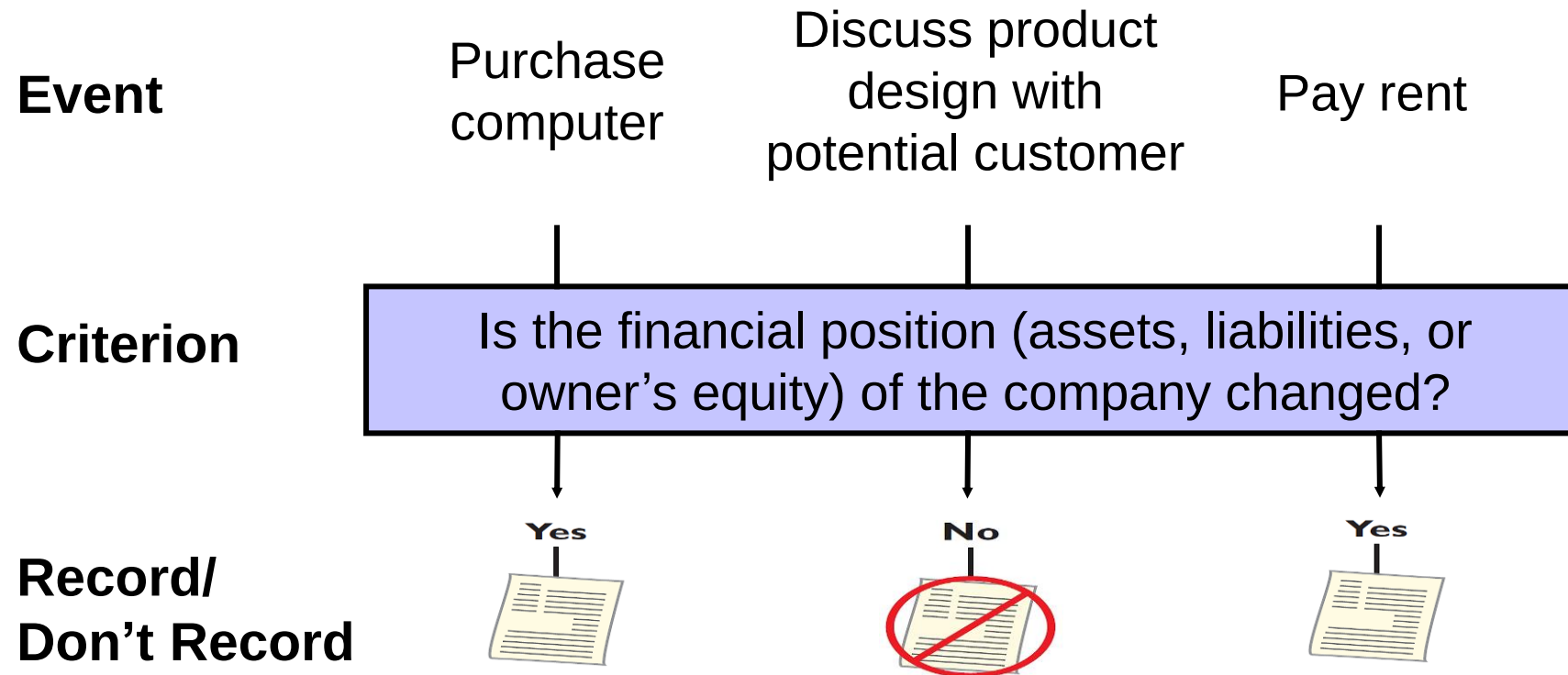
State the accounting equation, and define its components.

Classify the following items as investment by owner, owner's drawings, revenue, or expenses. Then indicate whether each item increases or decreases owner's equity.

	<u>Classification</u>	<u>Effect on Equity</u>
1. Drawings		
2. Salaries and Wages Expense		

Transaction Analysis

- ◆ Are the following events recorded in the accounting records?



Transaction Analysis

TRANSACTION 1. INVESTMENT BY OWNER Mohamed decides to start a smartphone app development company which he names Soft byte. On September 1, 2023, he invests **\$15,000 cash** in the business. This transaction results in an equal increase in assets and owner's equity.

	Assets				=	Liabilities +		Owner's Equity		
	Cash	+ Accounts Receivable	+ Supplies	+ Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+15,000						+15,000			

Transaction Analysis

TRANSACTION 2. PURCHASE OF EQUIPMENT FOR CASH Softbyte Inc. purchases computer equipment for **\$7,000 cash**.

Illustration 1-8

	Assets				= Liabilities +	Owner's Equity			
	Cash	+ Accounts Receivable	+ Supplies	+Equipment	= Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+15,000					+15,000			
2.	-7,000			+7,000					

Transaction Analysis

TRANSACTION 3. PURCHASE OF SUPPLIES ON CREDIT Softbyte Inc. purchases for \$1,600 headsets and other accessories expected to last several months. The supplier allows Softbyte to pay this bill in October.

	Assets				=	Liabilities		Owner's Equity			
	Cash	+ Accounts Receivable	+ Supplies	+ Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.	
1.	+15,000						+15,000				
2.	-7,000			+7,000							
3.			+1,600			+1,600					

Transaction Analysis

TRANSACTION 5. PURCHASE OF ADVERTISING ON CREDIT Softbyte Inc. receives a **bill for \$250** from the *Daily News* for advertising on its online website but postpones payment until a later date.

Illustration 1-8

Trans- action	Assets				= Liabilities +	Owner's Equity				
	Cash	+ Accounts Receivable	+ Supplies	+ Equipment	= Accounts Payable	+ Owner's Capital	+ Owner's Drawings	+ Rev.	- Exp.	
1.	+15,000					+15,000				
2.	-7,000			+7,000						
4.	+1,200							+1,200		
5.					+250				-250	

Transaction Analysis

TRANSACTION 6. SERVICES PERFORMED FOR CASH AND CREDIT.

Softbyte performs **\$3,500 of services**. The company receives **cash of \$1,500** from customers, and it bills the balance of **\$2,000 on account**.

Illustration 1-8	Assets				= Liabilities +		Owner's Equity			
	Cash	+ Accounts Receivable	+ Supplies	+ Equipment	= Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.	
1.	+15,000					+15,000				
2.	-7,000			+7,000						
3.			+1,600		+1,600					
4.	+1,200							+1,200		
5.					+250				-250	
6.	+1,500	+2,000						+3,500		

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Illustration 1-8

[illegible]

Transaction Analysis

TRANSACTION 8. PAYMENT OF ACCOUNTS PAYABLE Softbyte Inc. pays its \$250 *Daily News* bill in cash. The company previously (in Transaction 5) recorded the bill as an increase in Accounts Payable.

Trans- action	Assets				= Liabilities +	Owner's Equity			
	Cash	+ Accounts Receivable	+ Supplies	+Equipment	= Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+15,000					+15,000			
2.	-7,000			+7,000					
3.			+1,600		+1,600				
4.	+1,200							+1,200	
6.	+1,500	+2,000						+3,500	
7.	-1,700								-600
									-900
									-200
8.	-250				-250				

Transaction Analysis

TRANSACTION 9. RECEIPT OF CASH ON ACCOUNT Softbyte Inc.
receives \$600 in cash from customers who had been billed for services
(in Transaction 6).

Illustration 1-8

Trans- action	Assets				= Liabilities +		Owner's Equity		
	Cash	+ Accounts Receivable	+ Supplies	+ Equipment	= Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+15,000					+15,000			
2.	-7,000			+7,000					
3.			+1,600		+1,600				
4.	+1,200							+1,200	
6.	+1,500	+2,000						+3,500	
7.	-1,700								-600
									-900
									-200
8.	-250				-250				
9.	+600	-600							

TRANSACTION 10. WITHDRAWAL OF CASH BY OWNER Mohamed withdraws **\$1,300 in cash** in cash from the business for his personal use.

Illustration 1-8

Illustration 1-8		Assets				= Liabilities +	Owner's Equity			
Trans- action	Cash	+ Accounts Receivable	+ Supplies	+Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+15,000						+15,000			
2.	-7,000			+7,000						
3.			+1,600			+1,600				
4.	+1,200								+1,200	
5.						+250				-250
6.	+1,500	+2,000							+3,500	
7.	-1,700									-600
										-900
										-200
8.	-250					-250				
9.	+600	-600								
10.	-1,300							-1,300		
	\$18,050					\$18,050				

Summary of Transactions

1. Each transaction is analyzed in terms of its effect on:
 - a. The three components of the basic accounting equation.
 - b. Specific of items within each component.
2. The two sides of the equation must always be equal.

Transactions made by XY & Co., a public accounting firm, for the month of August are shown below. Prepare a tabular analysis which shows the effects of these transactions on the expanded accounting equation.

1. The owner invested \$25,000 cash in the business.
2. The company purchased \$7,000 of office equipment on credit.
3. The company received \$8,000 cash in exchange for services performed.
4. The company paid \$850 for this month's rent.
5. The owner withdrew \$1,000 cash for personal use.

Tabular Analysis

1. The owner invested \$25,000 cash in the business.

Assets		=	Liabilities +		Owner's Equity		
Cash	+ Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1. +25,000				+25,000			

2. The company purchased \$7,000 of office equipment on credit.

Trans- action	Assets		=	Liabilities +		Owner's Equity		
	Cash	+ Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+25,000				+25,000			
2.		+7,000		+7,000				

Tabular Analysis

3. The company received \$8,000 cash in exchange for services performed.

Trans- action	Assets		=	Liabilities +		Owner's Equity		
	Cash	+ Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+25,000				+25,000			
2.		+7,000		+7,000				
3.	+8,000						+8,000	

4. The company paid \$850 for this month's rent.

	Assets		=	Liabilities +		Owner's Equity		
	Cash	+ Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+25,000				+25,000			
2.		+7,000		+7,000				
3.	+8,000						+8,000	
4.	-850							-850

Tabular Analysis

5. The owner withdrew \$1,000 cash for personal use.

Trans- action	Assets		=	Liabilities +		Owner's Equity		
	Cash	+ Equipment	=	Accounts Payable	+ Owner's Capital	- Owner's Drawings	+ Rev.	- Exp.
1.	+25,000				+25,000			
2.		+7,000		+7,000				
3.	+8,000						+8,000	
4.	-850							-850
5.	-1,000					-1,000		
	<u>\$31,150</u>	<u>+</u> <u>\$7,000</u>	<u>=</u>	<u>\$7,000</u>	<u>+</u> <u>\$25,000</u>	<u>-</u> <u>\$1,000</u>	<u>+</u> <u>\$8,000</u>	<u>-</u> <u>\$850</u>
	<u>\$38,150</u>			<u>\$38,150</u>				

Questions:

The basic accounting equation may be expressed as

- a. **Assets = Equities.**
- b. **Assets – Liabilities = Owner's Equity.**
- c. **Assets = Liabilities - Owner's Equity.**
- d. **all of these**

Questions:

If total liabilities increased by \$15,000 and owner's equity increased by \$5,000 during a period of time, then total assets must change by what amount and direction during that same period?

- a. \$20,000 decrease
- b. \$20,000 increase
- c. \$25,000 increase
- d. \$30,000 increase

Questions:

If total liabilities decreased by \$15,000 and owner's equity increased by \$5,000 during a period of time, then total assets must change by what amount and direction during that same period?

- a. \$20,000 increase
- b. \$10,000 decrease
- c. \$10,000 increase
- d. \$15,000 decrease

Questions:

As of June 30, 2020, Habibo Company has assets of \$100,000 and owner's equity of \$5,000. What are the liabilities for Habibo Company as of June 30, 2020?

- a. \$85,000**
- b. \$90,000**
- c. \$95,000**
- d. \$100,000**

Questions:

Collection of a \$500 Accounts Receivable:

- a. increases an asset \$500; decreases an asset \$500.
- b. increases an asset \$500; decreases a liability \$500.
- c. decreases a liability \$500; increases owner's equity \$500.
- d. decreases an asset \$500; decreases a liability \$500.

Questions:

Classify each of the following items as owner's drawing (D), revenue (R), or expense (E).

(a) Advertising expense

(c) Insurance expense

(e) Bergman, Drawing

(g) Utilities expense

(b) Commission revenue

(d) Salaries expense

(f) Rent revenue

Tabular Analysis

Accounts payable

Cash

Cleaning equipment

Cleaning supplies

Accounts receivable

Notes payable

Salaries payable

Karin Meredith, Capital

Instructions

Classify each item as an asset, liability, or owner's equity.



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