

# Introduction to Financial Accounting and Financial Statements

## The Balance Sheet

Provides a list of all assets controlled by an entity and a list of how these assets are financed. Either through liabilities or shareholders' equity (aka a statement of financial position).

Assets	Liabilities & Shareholder's equity	
Current Assets	Current Liabilities	← Liabilities
	Noncurrent Liabilities	
Noncurrent Assets	Contributed Capital	← Shareholders' Equity
	Retained Earnings	

## The Accounting Equation

ASSETS	=	LIABILITIES	+	SHAREHOLDER'S	EQUITY
Economic Resources		Creditor's Claims on Assets		Shareholder's Claims on Assets	

## Definitions

### Asset

A resource controlled by the entity because of past events and from which future economic benefits are expected to flow to the entity

### Liability

A present obligation (obligation today) of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits (must use resources to settle the liability).

Examples include: accounts payable (invoices you receive, requiring payment), bank indebtedness (owing money to the bank on a short-term basis), dividends payable, returnable deposits, unearned revenues, sales taxes, employee related liabilities (wages payable), current portion of long-term debt (how much must be paid within the year), and long-term liabilities.

### Equity

The residual interest in the assets of the entity after deducting all its liabilities (assets – liabilities).

### Shareholder's Equity

Share capital (common shares) – the investment made by shareholders in the company.

*Retained earnings (end of year)*

$$\begin{aligned} &= \text{retained earnings (beginning of year)} + \text{net income for the year} \\ &\quad - \text{dividends declared to shareholders during the year} \end{aligned}$$

### Current Assets

Resources that are expected to be converted into cash, sold or consumed within a year or the operating cycle, whichever is longer.

Examples include: Cash, short-term investments (investing with a plan to liquidate within a year), accounts receivable (invoices you send, expecting payment), inventory, and prepaid expenses.

### Noncurrent assets

Assets that will be used up in the business for periods exceeding one year.

Examples include: long-term investments, tangible capital assets (land, buildings and equipment), and intangible capital assets (patents, trademarks, goodwill).

## Statement of Changes in Shareholders' Equity

This shows the change in each of the shareholders' equity items from the beginning of the year to the end of the year. It includes the following:

- Contributed capital (common stock/preferred stock)
  - Increases by new investments made by shareholders.
  - Decreases by repurchase of stock by company.

Private companies only need to present a statement of changes in retained earnings.

For the 52 weeks ended December 31, 2011 and January 1, 2011  
(in thousands of Canadian dollars)

	Note	Share Capital	Treasury Shares	Contributed Surplus	Accumulated Other Comprehensive Loss (Notes 18 and 21)	Retained Earnings	Total
Balance as at January 1, 2011 <sup>(1)</sup>		\$ 1,520,558	\$ –	\$ 11,702	\$ (8,643)	\$ 2,579,018	\$ 4,102,635
Total comprehensive income		–	–	–	(21,571)	613,934	592,363
Dividends	24	–	–	–	–	(215,671)	(215,671)
Share repurchases	24	(35,576)	(4,735)	–	–	(171,203)	(211,514)
Share-based payments	26	–	–	(1,210)	–	–	(1,210)
Share options exercised	26	1,466	–	(246)	–	–	1,220
Repayment of share-purchase loans		7	–	–	–	–	7
<b>Balance as at December 31, 2011</b>		<b>\$ 1,486,455</b>	<b>\$ (4,735)</b>	<b>\$ 10,246</b>	<b>\$ (30,214)</b>	<b>\$ 2,806,078</b>	<b>\$ 4,267,830</b>
Balance as at January 3, 2010 <sup>(1)</sup>		\$ 1,519,870	\$ –	\$ 10,274	\$ (1,125)	\$ 2,182,865	\$ 3,711,884
Total comprehensive income		–	–	–	(7,518)	591,851	584,333
Dividends	24	–	–	–	–	(195,698)	(195,698)
Share-based payments	26	–	–	1,592	–	–	1,592
Share options exercised	26	655	–	(164)	–	–	491
Repayment of share-purchase loans		33	–	–	–	–	33
<b>Balance as at January 1, 2011<sup>(1)</sup></b>		<b>\$ 1,520,558</b>	<b>\$ –</b>	<b>\$ 11,702</b>	<b>\$ (8,643)</b>	<b>\$ 2,579,018</b>	<b>\$ 4,102,635</b>

## ICP 1-1

## Question

The following is a list of accounts taken from the records of the Harrison Corporation as at December 31, 20x5:

Accounts Payable [CL]	22,500
Accounts Receivable [CA]	26,000
Accumulated Depreciation – Building	35,000
Accumulated Depreciation – Equipment	15,000
Building [LTA]	140,000
Capital Stock [SE]	50,000
Cash [CA]	11,000
Equipment [LTA]	56,000
Interest Payable [CL]	1,500
Inventory [CA]	46,000
Land [LTA]	25,000
Long-term Debt [LTD]	80,000
Long-Term Investments [LTA]	10,000
Office supplies [CA]	4,500
Patents [LTA]	30,000
Retained Earnings [SE]	141,000
Salaries Payable [CL]	3,500

Prepare a classified statement of financial position as at December 31, 20x5.

## Solution

Harrison Corporation  
Statement of Financial Position  
As of December 31, 20x5

## Assets:

## Current Assets

Cash		11,000
Accounts Receivable		26,000
Inventory		46,000
Office supplies		4,500
Total Current Assets		87,500

## Long-Term Assets

Long-Term Investments		10,000
Land		25,000
Building	140,000	
less accumulated depreciation	<u>(35,000)</u>	105,000
Equipment	56,000	
less accumulated depreciation	<u>(15,000)</u>	41,000
Patents		30,000
Total Long-Term Assets		211,000

Total Assets	298,500
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## Liabilities:

## Shareholders' Equity

## Current Liabilities

Accounts Payable	22,500
Interest Payable	1,500
Salaries Payable	3,500
Total Current Liabilities	27,500

Long-Term Debt	80,000
Total Liabilities	107,500

## Shareholders' Equity

Capital Stock	50,000
Retained Earnings	141,000
Total Shareholder's Equity	191,000

Total Liabilities	298,500
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## The Income Statement

The income statement provides the results of operation (profitability) for a period of time, usually one year. The typical format is:

Sales  
 - Cost of goods sold  
 = Gross profit or Gross margin  
 - Operating Expenses  
 = Operating Income  
 +- Other expense/revenues  
 = Net income before taxes  
 - Income tax expense  
 = Net income

### ICP 1-2

The following are taken from the accounts for the Noble Corporation for the year ended December 31, 20x8:

<del>Accounts receivable</del>	<del>38,500</del>
<del>Accumulated depreciation</del>	<del>56,000</del>
Cost of goods sold	500,000
Depreciation expense [OER]	68,000
Income tax expense [IT]	35,000
Insurance expense [OE]	16,800
Interest expense [OER]	20,000
Interest revenue [OER]	15,000
<del>Land [OER]</del>	<del>45,000</del>
Miscellaneous expenses [OER]	6,000
<del>Office Supplies [OI]</del>	<del>4,800</del>
Office supplies expense [OE]	5,600
Rent expense [OP]	96,000
Salaries expense [OE]	165,000
Sales	950,000

Prepare an income statement for Noble Corporation.

**Solution**

Noble Corporation

Statement of income

For year ended December 31, 20x8

Sales		950,000
Cost of goods sold	<u>(500,000)</u>	
Gross profit		450,000
Insurance expense	(16,800)	
Office supplies expense	(5,600)	
Salaries expense	<u>(165,000)</u>	262,600
Depreciation expense	(68,000)	
Interest expense	(20,000)	
Interest revenue		15,000
Land		45,000
Miscellaneous expenses	<u>(6,000)</u>	228,600
Income tax expense	<u>(35,000)</u>	193,600

## ICP 1-3

**ICP 1-3**

The following is an alphabetical list of account balances at December 31, 20x3 for the Peters Corporation. You are also told that the company issued \$250,000 of Capital Stock during the year and declared a total of \$50,000 of dividends.

Accounts payable	136,000
Accounts Receivable	89,000
Accumulated depreciation – building	389,000
Accumulated depreciation – equipment	151,000
Building	1,116,000
Capital Stock	612,000
Cash	48,000
Cost of goods sold	756,000
Depreciation expense	58,000
Dividends payable	7,000
Franchise	29,000
Income tax expense	65,000
Insurance expense	4,000
Interest expense	54,000
Interest income	7,000
Interest payable	12,000
Interest receivable	9,000
Inventories	155,000
Land	202,000
Long-term debt	720,000
Long-term investments	25,000
Machinery and equipment	615,000
Patents	109,000
Prepaid expenses	12,000
Rent expense	11,000
Rental revenues	36,000
Retained Earnings (beginning of year balance less dividends)	220,000
Salaries expense	115,000
Sales	1,370,000
Short-term investments	131,000
Unearned revenues	43,000

***Required -***

Prepare a Statement of Income, a Statement of Financial Position and a statement of changes in Shareholders' Equity.



## Statement of Changes in Shareholders Equity

Shows the change in each of the shareholder's equity from the beginning of the year to the end of the year.