Updates

- ❑ **TA Office Hours – C00**
  - ➢ **This week**
    - ➢ **Tuesday 3-4pm, Office 2E124**
    - ➢ **Friday 1-2pm, Office 2E124**
  - ➢ **Going forward**
    - ➢ **Tuesdays 3-4pm, Office 2E124**
    - ➢ **By appointment: Email Stephanie**

Class Outline

❑ **Achieving the Objective**

	Topics
Week 1	Financial Accounting Framework ✓
Week 2	Double-entry mechanics
Week 3	The Accounting Cycle
Week 4	Accounts Receivable
Week 5	Inventories
Week 6	MIDTERM EXAM
Week 7	Long-Term Assets
Week 8	Accounting Fraud
Week 9	Liabilities
Week 10	Accounting Transactions
Finals Week	FINAL EXAM

❑ **Economic activity is complex…..accounting requires judgment and critical thinking**

FINANCIAL ACCOUNTING FRAMEWORK

RECAP

Objective: Week 1 Refresher

Accounting

❑ **Financial Statements – company's periodic reports – (Communication)**

➢ Balance Sheet
- At start of period ✓
- At end of year ✓

➢ Income Statement
- For the year ✓

➢ Statement of Stockholders' Equity
- For the year ✓

➢ Statement of Cash Flows
- For the year ✓
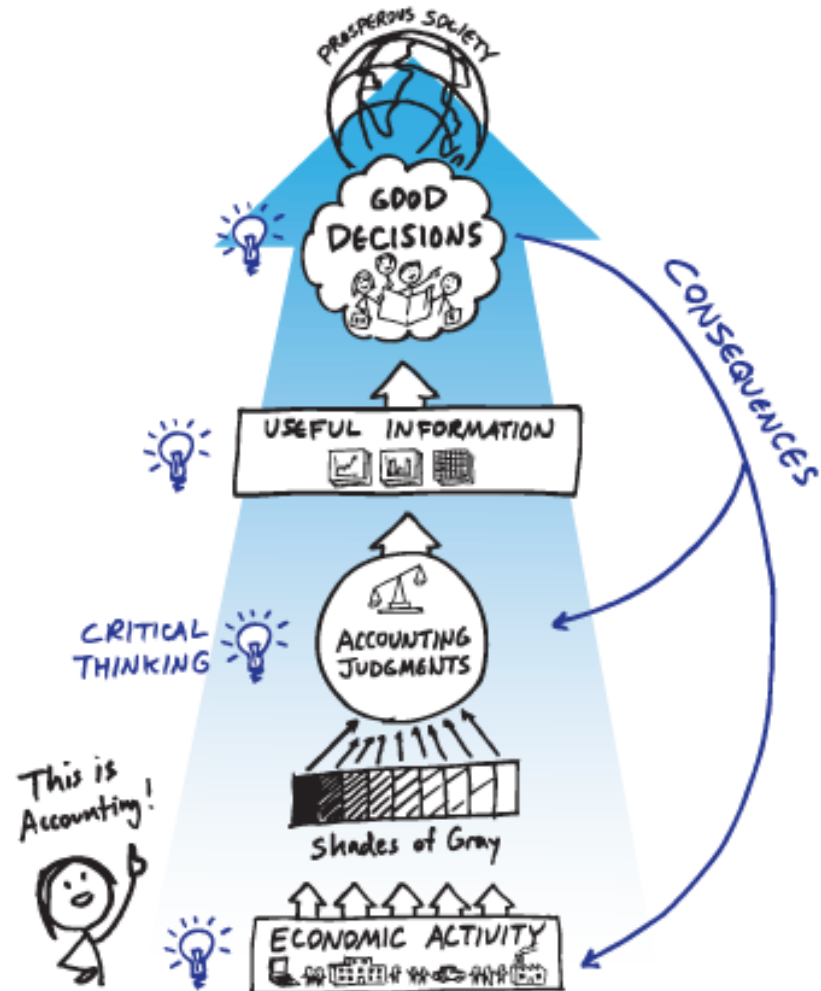
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❑ **Financial Statements – company's periodic reports – (Communication)**

➤ Balance Sheet
- At start of period ✔
- At end of year ✔

➤ Income Statement
- For the year ✔

➤ Statement of Stockholders' Equity
- For the year ✔

➤ Statement of Cash Flows
- For the year ✔

Details about the change between two balance sheet dates

Linking the F/S

❑ **Financial Statements – company's periodic reports – (Communication)**

➢ Balance Sheet

- At start of period ✓
- At end of year ✓

➢ Income Statement

- Details about resource flows
  Generating value

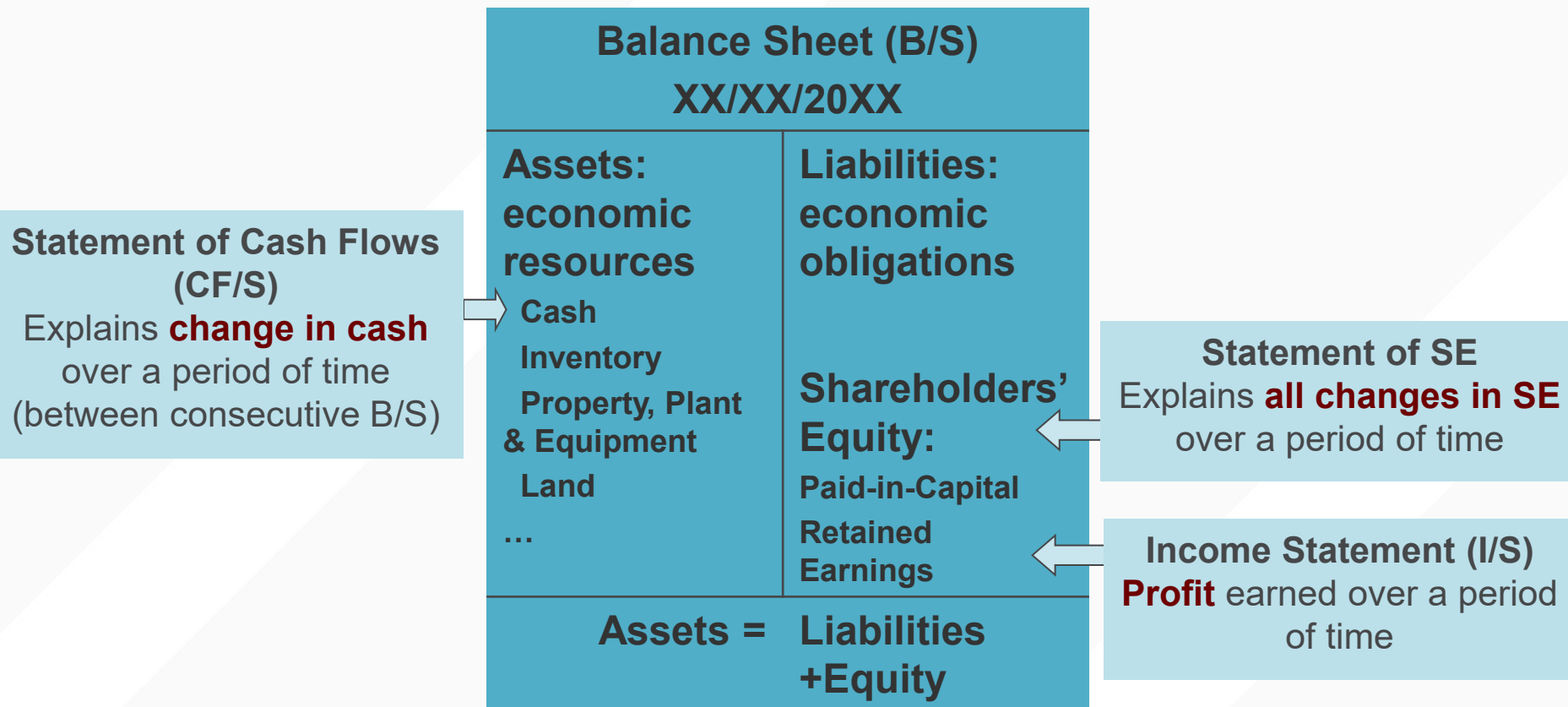➢ Statement of Stockholders' Equity

- Changes in the equity

➢ Statement of Cash Flows

- Changes in the cash

Details about the change between two balance sheet dates

Linking the F/S

❑ **Financial Statements – company's periodic reports – (Communication)**

Statement of Cash Flows (CF/S)
Explains **change in cash** over a period of time (between consecutive B/S)

Balance Sheet (B/S)
XX/XX/20XX

Assets: economic resources	Liabilities: economic obligations
Cash	
Inventory	
Property, Plant & Equipment	**Shareholders' Equity:**
Land	Paid-in-Capital
...	Retained Earnings

Assets = Liabilities +Equity

Statement of SE
Explains **all changes in SE** over a period of time

Income Statement (I/S)
Profit earned over a period of time

Financial statements do not exist in isolation: link between B/S, I/S, CF/S and Statement of Shareholders' Equity!

Financial Statements

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2018 FORM 10-K

❑ **How they link:**

[1]

($ millions)

Balance Sheet
May 31, 2017

Assets
Cash . . . . $ 3,808
Noncash assets 19,451

Total assets $23,259

Liabilities and equity
Liabilities $10,852
Stockholders' equity 12,407

Total liabilities and equity . . . $23,259

Statement of Cash Flows
For Year Ended May 31, 2018

Operating cash flows . . . . . . $ 4,955
Investing cash flows 276
Financing cash flows . . . . . . (4,835)
Exchange rate changes 45

Increase (decrease)
in cash 441
Cash, May 31, 2017 3,808
Cash, May 31, 2018 . . . . $ 4,249

[5]

[6]

Balance Sheet
May 31, 2018

Assets
Cash . . . . $ 4,249
Noncash assets 18,287

Total assets $22,536

Liabilities and equity
Liabilities $12,724
Stockholders' equity 9,812

Total liabilities and equity . . . $22,536

Income Statement
For Year Ended May 31, 2018

Revenues $36,397
Expenses 34,464

Net income . . . . $ 1,933

[3]

Statement of Stockholders' Equity
For Year Ended May 31, 2018

Stockholders' equity,
May 31, 2017 . . . . $12,407
Net income 1,933
Dividends . . . . (1,265)
Stock issuances and
other . . . . (3,263)
Stockholders' equity
May 31, 2018 . . . . $9,812

[2]

[4]

| Point in time (Beginning of year) | Period of time (Fiscal year) | Point in time (End of year) |

Financial Statements

NIKE 2018 FORM 10-K

☐ **Net Income = ⇧ SE**

☐ **Net Loss = ⇩ SE**

Balance Sheet
May 31, 2018

Assets	
Cash	$ 4,249
Noncash assets	18,287
Total assets	$22,536

Liabilities and equity	
Liabilities	$12,724
Stockholders' equity	9,812
Total liabilities and equity . . .	$22,536

Income Statement
For Year Ended May 31, 2018

Revenues	$36,397
Expenses	34,464
Net income	$ 1,933

[3]

Statement of Stockholders' Equity
For Year Ended May 31, 2018

Stockholders' equity, May 31, 2017	$12,407
Net income	1,933
Dividends	(1,265)
Stock issuances and other	(3,263)
Stockholders' equity May 31, 2018	$9,812

[4]

Point in time (Beginning of year)	Period of time (Fiscal year)	Point in time (End of year)

Financial Statements

NIKE 2018 FORM 10-K

- ❑ **Revenues = ⇧ SE**
- ❑ **Expenses = ⇩ SE**

[3]

Income Statement For Year Ended May 31, 2018	
Revenues	$36,397
Expenses	34,464
Net income	$ 1,933

Statement of Stockholders' Equity For Year Ended May 31, 2018	
Stockholders' equity, May 31, 2017	$12,407
Net income	1,933
Dividends	(1,265)
Stock issuances and other	(3,263)
Stockholders' equity May 31, 2018	$9,812

Point in time (Beginning of year)	Period of time (Fiscal year)	Point in time (End of year)

Financial Statements

- **Revenues = ⇧ SE**
- **Expenses = ⇩ SE**

DOUBLE ENTRY RECORDKEEPING

Objective: Understand the dual-entry recording framework and learn to use it to record a series of transactions
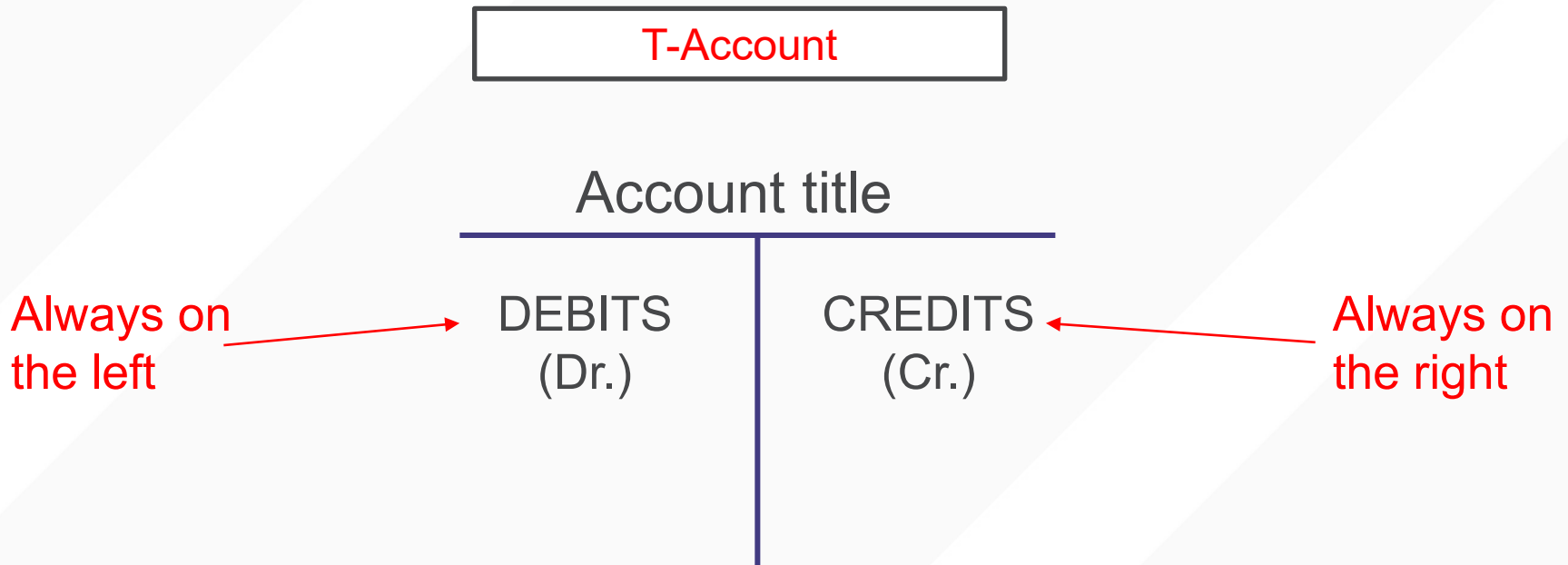
Double-entry Accounting

❑ **Every economic event has two sides, a give and a take**

❑ **Record both sides of economic events as a *transaction***

$$\text{Assets} \quad = \quad \text{Liabilities} \quad + \quad \text{Stockholders' Equity}$$

❑ **Every transaction will affect at least one of these classes: A, L, or SE**

❑ **Accounting equation must always be balanced ➔ The two sides of a transaction must balance**

Double-entry Accounting

❑ **Each transaction (economic event) will have a <u>dual effect</u>**

❑ **How do we increase and decrease the account balances?**

- ➢ Debits and credits
    - • Debit ➔ left
    - • Credit ➔ right
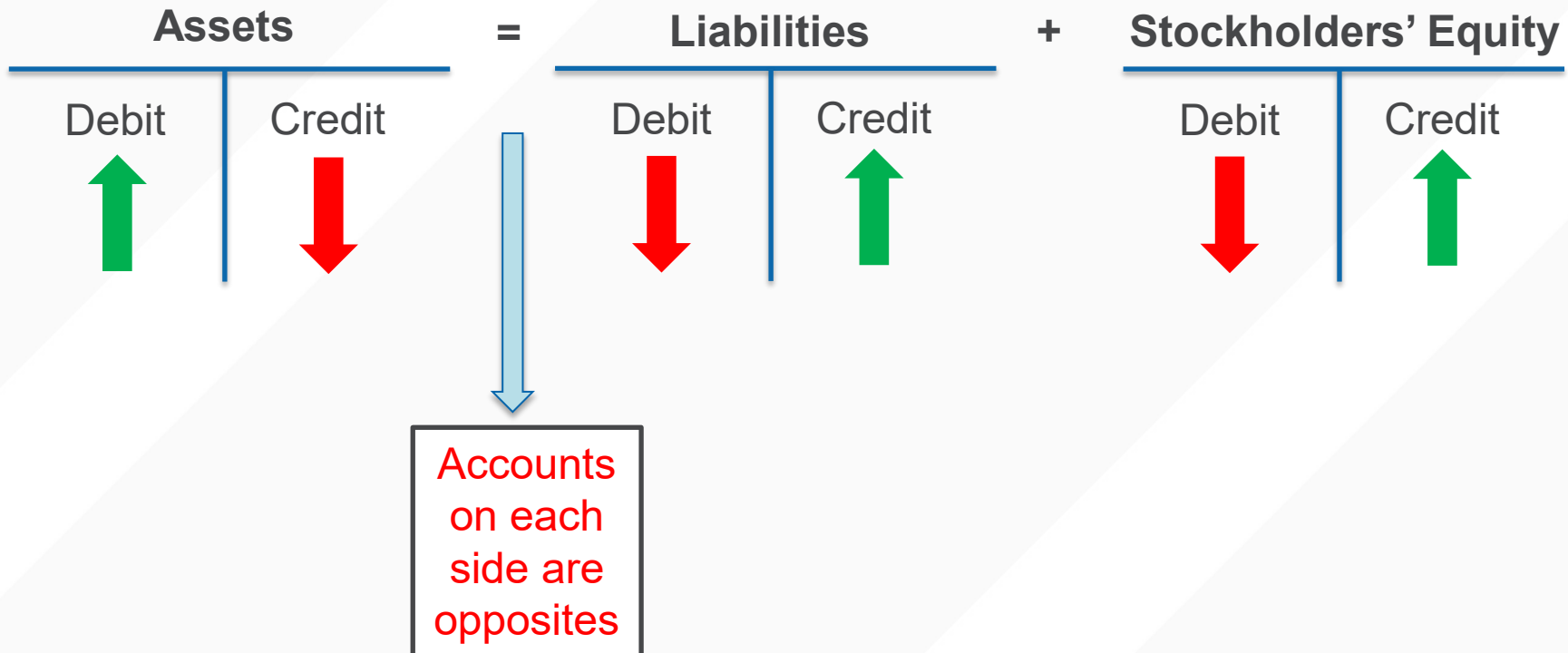
> T-Account

Account title

| DEBITS (Dr.) | CREDITS (Cr.) |

Always on the left →

← Always on the right

Double-entry Accounting

❑ **One side of the T-account is used to record increases to the account, and the other side is used to record decreases to the account.**

Assets		**=**	**Liabilities**		**+**	**Stockholders' Equity**	
Debit	Credit		Debit	Credit		Debit	Credit
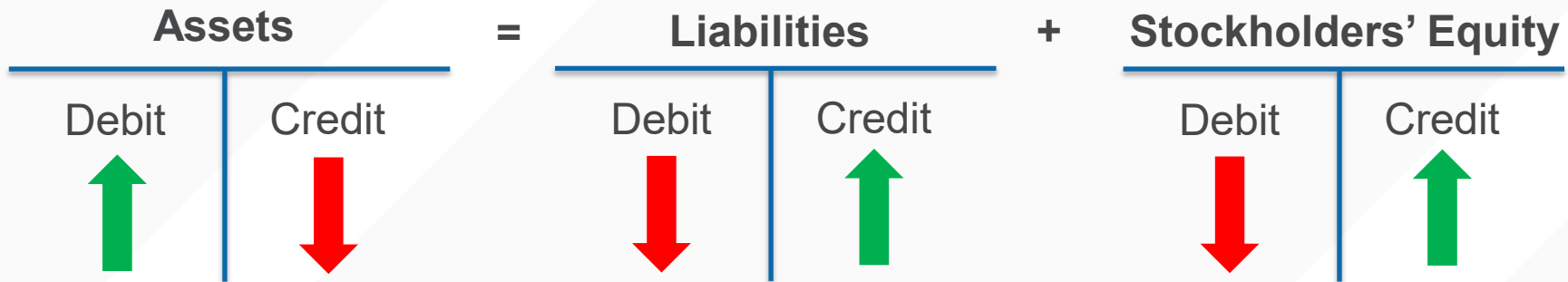
➤ A **debit** increases *assets* and decreases *liabilities and SE*

➤ A **credit** decreases *assets* and increases *liabilities and SE*

Double-entry Accounting

❑ **One side of the T-account is used to record increases to the account, and the other side is used to record decreases to the account.**

Assets		=	Liabilities		+	Stockholders' Equity	
Debit	Credit		Debit	Credit		Debit	Credit
↑	↓		↓	↑		↓	↑

Accounts on each side are opposites

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❑ **Rules of Debits and Credits**

➤ No negative numbers are allowed.

- We use debit (Dr) and credit (Cr)

➤ Every transaction must have at *least* one debit and at least one credit

➤ Debits must equal credits for all transactions.

- If you increase one you must increase another

Debits = Credits

Double-entry Accounting

	Transaction	Assets =	Liability +	Equity
1.	Local bank loans you $100,000.	+$100,000	+$100,000	
2.	Purchase equipment for $60,000 cash.			
3.	Purchase inventory for $15,000 on account.			
4.	Pay supplier $8,000 cash of the $15,000 owed.			
5.	Pay for one year insurance policy, $600 in cash.			

Double-entry Accounting

❑ **Local bank loans you $100,000.**

DEBIT   CREDIT

CASH

100,000

NOTES PAYABLE

100,000

Double-entry Accounting

	Transaction	Assets =	Liability +	Equity
1.	Local bank loans you $100,000.	+$100,000	+$100,000	
2.	Purchase equipment for $60,000 cash.	+$60,000 -$60,000		
3.	Purchase inventory for $15,000 on account.			
4.	Pay supplier $8,000 cash of the $15,000 owed.			
5.	Pay for one year insurance policy, $600 in cash.			

Double-entry Accounting

❑ **Purchase equipment for $60,000 cash**

DEBIT   CREDIT

CASH

[1] 100,000

NOTES PAYABLE

100,000 [1]

Double-entry Accounting

☐ **Purchase equipment for $60,000 cash**

DEBIT   CREDIT

CASH
[1] 100,000 | 60,000

NOTES PAYABLE
| 100,000 [1]

EQUIPMENT
60,000 |

Double-entry Accounting

	Transaction	Assets =	Liability +	Equity
1.	Local bank loans you $100,000.	+$100,000	+$100,000	
2.	Purchase equipment for $60,000 cash.	+$60,000 -$60,000		
3.	Purchase inventory for $15,000 on account.	+$15,000	+$15,000	
4.	Pay supplier $8,000 cash of the $15,000 owed.			
5.	Pay for one year insurance policy, $600 in cash.			

Double-entry Accounting

☐ **Purchase inventory for $15,000 on account.**

DEBIT   CREDIT

CASH

[1] 100,000   60,000 [2]

NOTES PAYABLE

100,000 [1]

EQUIPMENT

[2] 60,000

TRADE PAYABLE

15,000

INVENTORY

15,000

Double-entry Accounting

	Transaction	Assets =	Liability +	Equity
1.	Local bank loans you $100,000.	+$100,000	+$100,000	
2.	Purchase equipment for $60,000 cash.	+$60,000 -$60,000		
3.	Purchase inventory for $15,000 on account.	+$15,000	+$15,000	
4.	Pay supplier $8,000 cash of the $15,000 owed.	-$8,000	-$8,000	
5.	Pay for one year insurance policy, $600 in cash.			

Double-entry Accounting

☐ **Pay supplier $8,000 cash of the $15,000 owed.**

DEBIT   CREDIT

CASH

[1] 100,000	60,000 [2]
	8,000

NOTES PAYABLE

	100,000 [1]

EQUIPMENT

[2] 60,000	

TRADE PAYABLE

8,000	15,000 [3]

INVENTORY

[3] 15,000	

Double-entry Accounting

	Transaction	Assets =	Liability +	Equity
1.	Local bank loans you $100,000.	+$100,000	+$100,000	
2.	Purchase equipment for $60,000 cash.	+$60,000 -$60,000		
3.	Purchase inventory for $15,000 on account.	+$15,000	+$15,000	
4.	Pay supplier $8,000 cash of the $15,000 owed.	-$8,000	-$8,000	
5.	Pay for one year insurance policy, $600 in cash.	+$600 -$600		

Double-entry Accounting

☐ **Pay for one year insurance policy, $600 in cash.**

DEBIT   CREDIT

CASH

[1] 100,000	60,000 [2]
	8,000 [4]
	600

PREPAID INSURANCE

600

EQUIPMENT

[2] 60,000

NOTES PAYABLE

	100,000 [1]

INVENTORY

[3] 15,000

TRADE PAYABLE

[4] 8,000	15,000 [3]

Accounting Equation

❑ **Let's expand the equation**

$$\boxed{\text{Assets}} = \boxed{\text{Liab-ilities}} \quad + \quad \boxed{\text{Shareholders' Equity}}$$

Accounting Equation

❑ **Let's expand the equation**

$$\boxed{\text{Assets}} = \boxed{\text{Liab-ilities}} + \boxed{\text{Shareholders' Equity}}$$

$$\boxed{\text{Assets}} = \boxed{\text{Liab-ilities}} + \boxed{\text{Contri-buted Capital}} + \boxed{\text{Retained Earning}}$$

Accounting Equation

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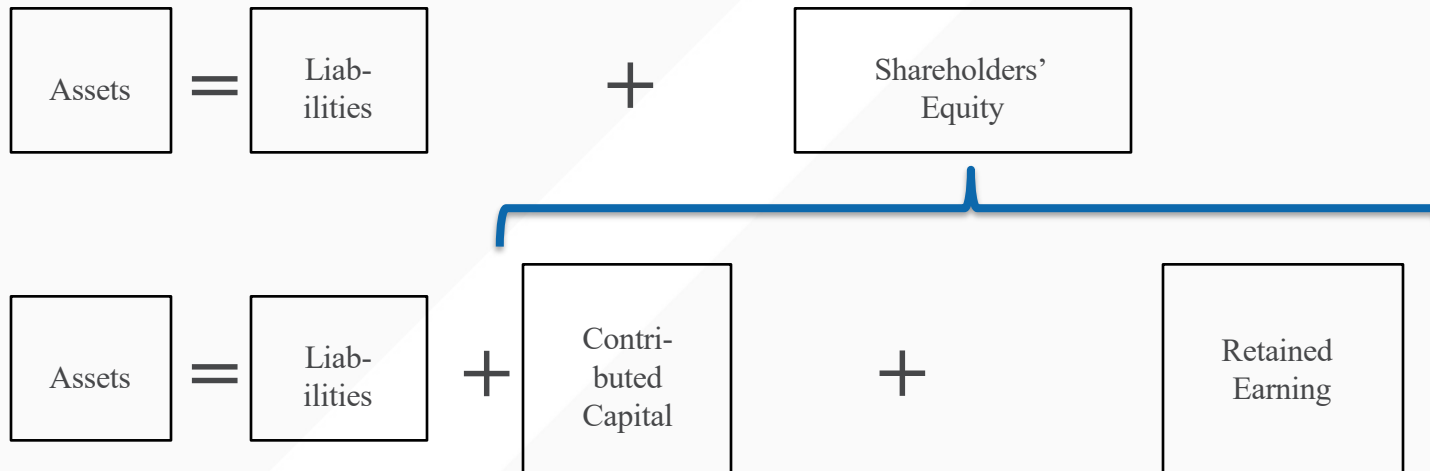
❑ **Let's expand the equation**

Accounting Equation

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❑ **Let's expand the equation**

| Assets | = | Liab-ilities | + | Shareholders' Equity |

| Assets | = | Liab-ilities | + | Contri-buted Capital | + | Retained Earning |

| Assets | = | Liab-ilities | + | Contri-buted Capital | + | Retained Earning Beginning of Period | + | Net Income for period | − | Dividends for period |

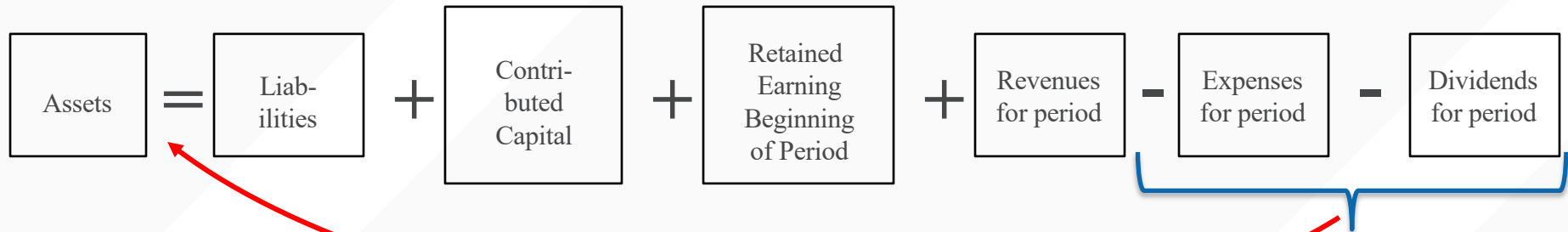| Assets | = | Liab-ilities | + | Contri-buted Capital | + | Retained Earning Beginning of Period | + | Revenues for period | − | Expenses for period | − | Dividends for period |

Accounting Equation

❑ **Let's expand the equation**

$$\text{Assets} = \text{Liabilities} + \text{Contributed Capital} + \text{Retained Earning Beginning of Period} + \text{Revenues for period} - \text{Expenses for period} - \text{Dividends for period}$$

❑ **And then rearrange the equation:**

$$\text{Assets} = \text{Liabilities} + \text{Contributed Capital} + \text{Retained Earning Beginning of Period} + \text{Revenues for period} - \text{Expenses for period} - \text{Dividends for period}$$

❑ **Rearranged:**

$$\text{Assets} + \text{Expenses for period} + \text{Dividends for period} = \text{Liabilities} + \text{Contributed Capital} + \text{Retained Earning Beginning of Period} + \text{Revenues for period}$$

Double-entry Accounting

❑ **Rearranged equation:**

$$\text{Assets} + \text{Expenses for period} + \text{Dividends for period} = \text{Liab-ilities} + \text{Contri-buted Capital} + \text{Retained Earning Beginning of Period} + \text{Revenues for period}$$
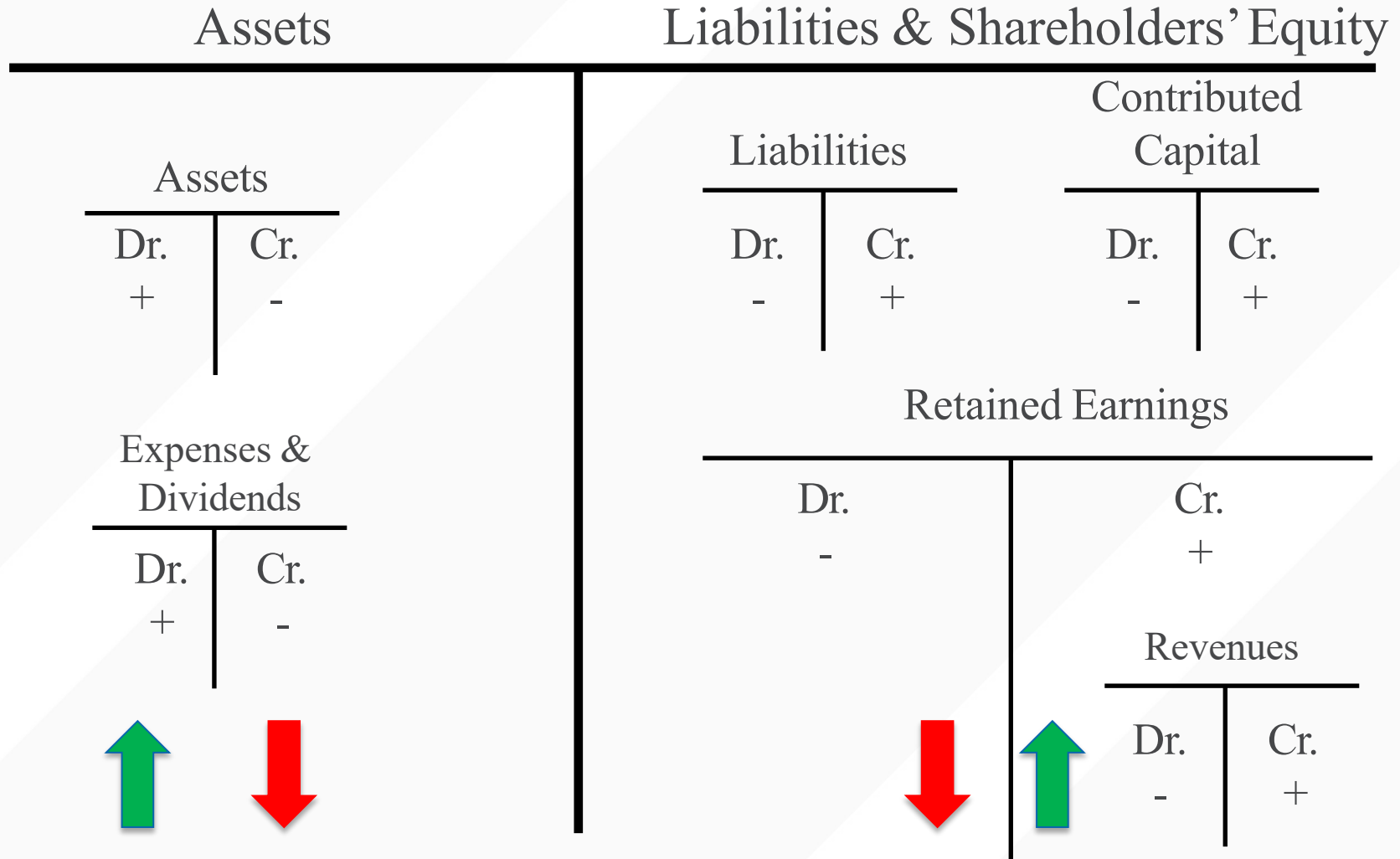
DEBIT   CREDIT

Accounts on each side are opposites

DEBIT   CREDIT
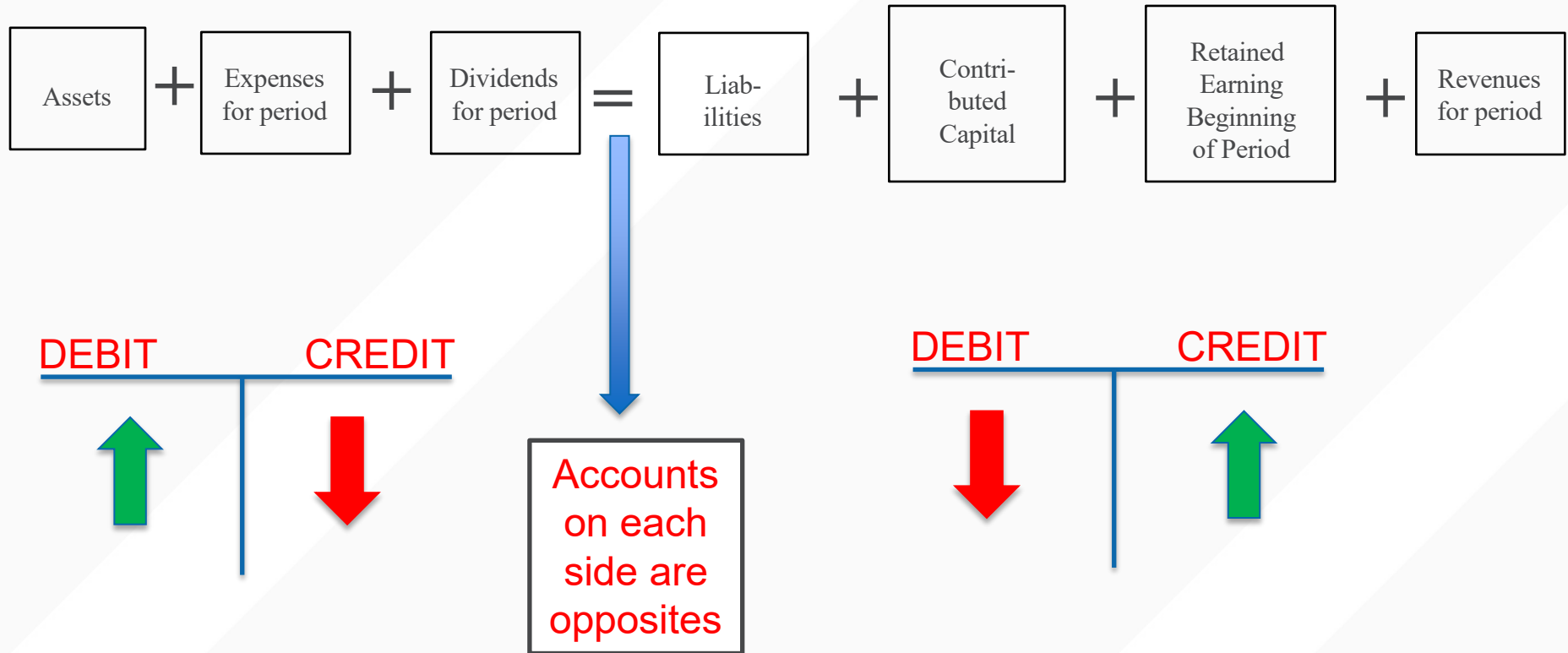
Double-entry Accounting

❑ **Super T-account**

Double-entry Accounting

❑ **If you get stuck:**

D E A L O R

Dividends   **L**iabilities
Expenses   **O**wners' Equity
Assets   **R**evenue

Debit   ⬆   ⬇   Debit

Credit   ⬇   ⬆   Credit

Double-entry Accounting

	Transaction	Assets =	Liability +	Equity
1.	Local bank loans you $100,000.	+$100,000	+$100,000	
2.	Purchase equipment for $60,000 cash.	+$60,000 -$60,000		
3.	Purchase inventory for $15,000 on account.	+$15,000	+$15,000	
4.	Pay supplier $8,000 cash of the $15,000 owed.	-$8,000	-$8,000	
5.	Pay for one year insurance policy, $600 in cash.	+$600 -$600		
6.	Issue 10,000 shares for $100,000.	+$100,000		+$100,000

Double-entry Accounting

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☐ **Issue 10,000 shares for $100,000.**

DEBIT   CREDIT

CASH
[1] 100,000	60,000 [2]
100,000	8,000 [4]
	600 [5]

PREPAID INSURANCE
[5] 600	

EQUIPMENT
[2] 60,000	

COMMON STOCK
	100,000

INVENTORY
[3] 15,000	

NOTES PAYABLE
	100,000 [1]

TRADE PAYABLE
[4] 8,000	15,000 [3]

Double-entry Accounting

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❑ **Let's calculate ending balances**

	DEBIT	CREDIT

CASH

100,000	60,000
100,000	8,000
	600

PREPAID INSURANCE

600	

EB 600

EQUIPMENT

60,000	

EB 60,000

COMMON STOCK

	100,000

100,000 EB

NOTES PAYABLE

	100,000

100,000 EB

TRADE PAYABLE

8,000	15,000

INVENTORY

15,000	

EB 15,000

EB = Ending balance

Double-entry Accounting

UC San Diego
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❑ **Let's calculate ending balances**

DEBIT   CREDIT

CASH

100,000	60,000
100,000	8,000
	600

PREPAID INSURANCE

| 600 | |

EB 600

NOTES PAYABLE

| | 100,000 |
| | 100,000 EB |

EQUIPMENT

| 60,000 | |

EB 60,000

COMMON STOCK

| | 100,000 |
| | 100,000 EB |

INVENTORY

| 15,000 | |

EB 15,000

EB = Ending balance

TRADE PAYABLE

| 8,000 | 15,000 |

Double-entry Accounting

DEBIT   CREDIT

❑ **Let's calculate ending balances**

❑ **The T-account is a useful representation of the equation:**

     BB + account increases − account decreases = EB

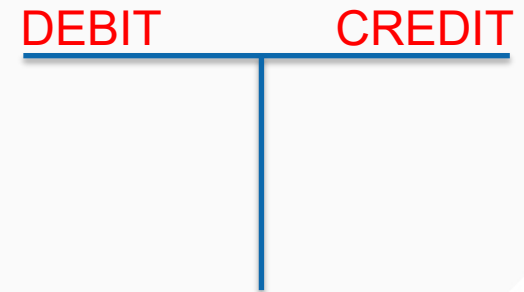❑ **Trade payable is a liability ➔ debit decreases the liability**
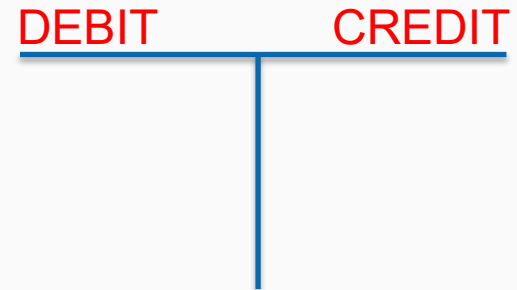
TRADE PAYABLE

8,000	15,000
	7,000 EB

= 15,000 − 8,000 = 7,000 CREDIT

BB = Beginning balance
EB = Ending balance

Double-entry Accounting

❑ Let's calculate ending balances

❑ Cash is an **asset** ➔ credit decreases cash

DEBIT   CREDIT

CASH

100,000	60,000
100,000	8,000
	600

200,000   68,600

EB 131,400

= 200,000 – 68,600 = 131,400 DEBIT

EB = Ending balance

Double-entry Accounting

☐ **These ending balances will be on the balance sheet**

	DEBIT	CREDIT

CASH

100,000	60,000
100,000	8,000
	600

EB **131,400**

EQUIPMENT

60,000	

EB **60,000**

INVENTORY

15,000	

EB **15,000**

PREPAID INSURANCE

600	

EB **600**

COMMON STOCK

	100,000

100,000 EB

EB = Ending balance

NOTES PAYABLE

	100,000

100,000 EB

TRADE PAYABLE

8,000	15,000

7,000 EB

Double-entry Accounting

☐ **These ending balances will be on the balance sheet**

☐ **They'll be the beginning balances at the start of the next period**
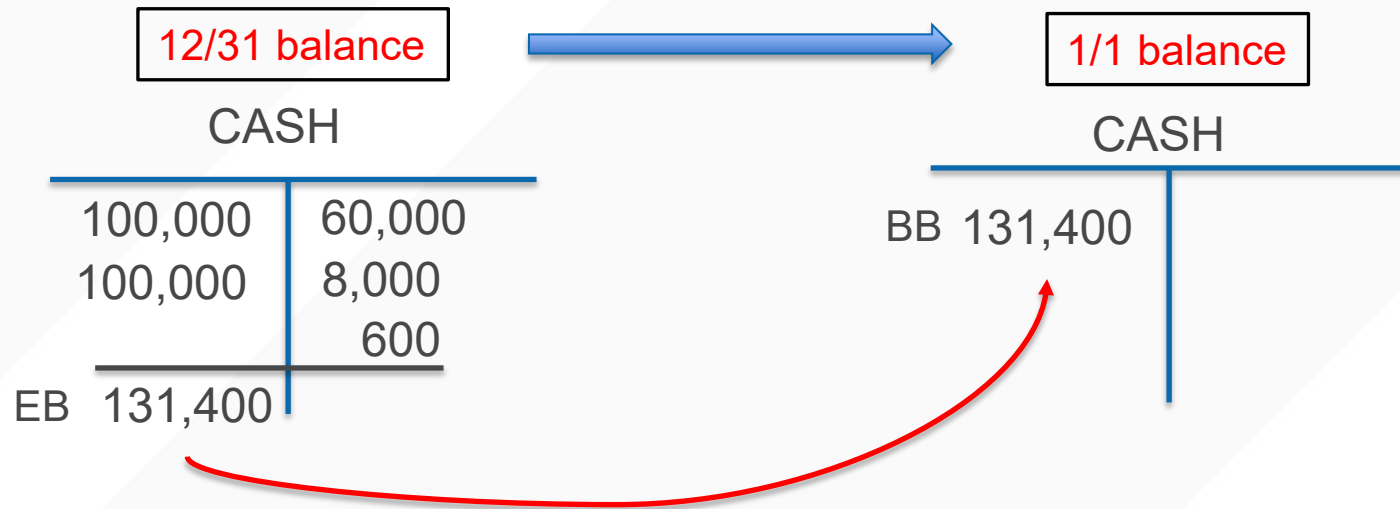
DEBIT   CREDIT

| 12/31 balance | → | 1/1 balance |

CASH

100,000	60,000
100,000	8,000
	600

EB 131,400

CASH

BB 131,400

BB = Beginning Balance
EB = Ending balance

Double-entry Accounting

❑ **These ending balances will be on the balance sheet**

❑ **They will the beginning balances at the start of the next period**

DEBIT   CREDIT

CASH

BB 131,400

PREPAID INSURANCE

BB 600

NOTES PAYABLE

100,000 BB

EQUIPMENT

BB 60,000

COMMON STOCK

100,000 BB

TRADE PAYABLE

7,000 BB

INVENTORY

BB 15,000

BB = Beginning balance

Double-entry Accounting

❑ **Transactions are recorded as journal entries**

➢ Same transaction rules apply:

- We use debit (Dr) and credit (Cr).

- Debits must equal credits for all transactions.

➢ Debits are recorded first, then indent the credit account

Debits = Credits

Double-entry Accounting

□ **Example: (1) On December 8, investors contributed $10,000 cash to start La Colombiana Coffee Roasters, in exchange for 1,000 shares of stock**

Record debits first.

Debit amounts go in the left column

(1) Cash	10,000

➢ Each posting in the T-account is accompanied by the number of the transaction for easier tracking

Double-entry Accounting

❑ **Example: On December 8, investors contributed $10,000 cash to start La Colombiana Coffee Roasters, in exchange for 1,000 shares of stock**

Credit account names are indented from the left margin.		Credit amounts go in the right column

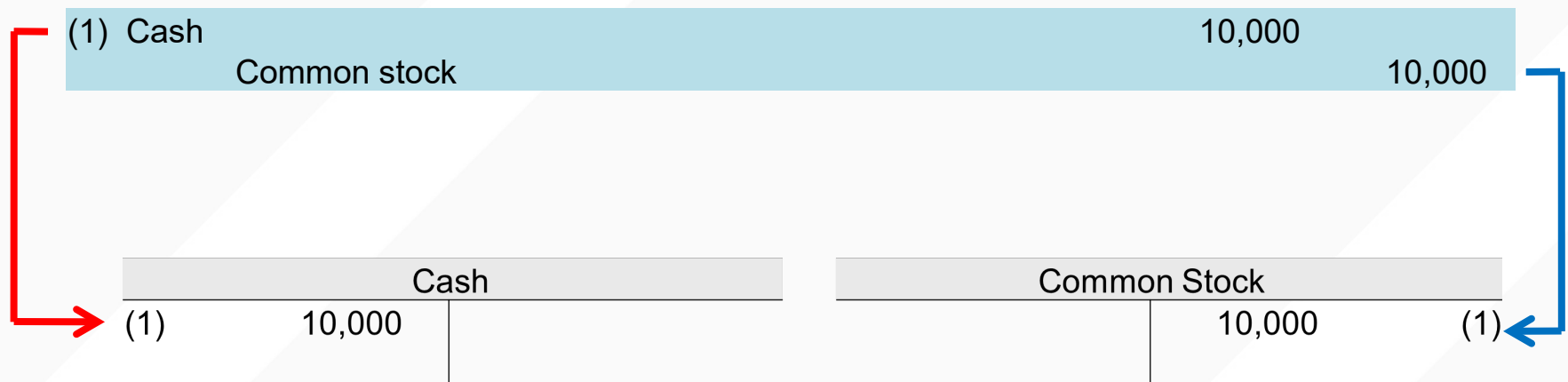| (1) Cash	10,000	
Common stock		10,000

Double-entry Accounting

❑ **Example: On December 8, investors contributed $10,000 cash to start La Colombiana Coffee Roasters, in exchange for 1,000 shares of stock**

(1) Cash	10,000	
Common stock		10,000

Cash			Common Stock	
(1)	10,000		10,000	(1)

Double-entry Accounting

❑ **Example: La Colombiana buys inventory for $200**

(2)	Inventory	200	
	Cash		200

Double-entry Accounting

❑ **Example: Jana Juice buys inventory for $200**

(2) Inventory		200
Cash		200

Cash			Common Stock	
(1) 10,000			10,000	(1)
	(2) 200			

Inventory

(2) 200

Double-entry Accounting

❑ **Let's record these transactions as journal entries**

	Transaction	Assets =	Liability +	Equity
1.	Local bank loans you $100,000.	+$100,000	+$100,000	
2.	Purchase equipment for $60,000 cash.	+$60,000 -$60,000		
3.	Purchase inventory for $15,000 on account.	+$15,000	+$15,000	
4.	Pay supplier $8,000 cash of the $15,000 owed.	-$8,000	-$8,000	
5.	Pay for one year insurance policy, $600 in cash.	+$600 -$600		
6.	Issue 10,000 shares for $100,000.	+$100,000		+$100,000

Double-entry Accounting

❑ **Let's record these transactions as journal entries**

	Transaction		
1.	Local bank loans you $100,000.	(1) Cash	100,000
		Notes Payable	100,000
2.	Purchase equipment for $60,000 cash.	(2) Equipment	60,000
		Cash	60,000
3.	Purchase inventory for $15,000 on account.	(3) Inventory	15,000
		Account Payable	15,000
4.	Pay supplier $8,000 cash of the $15,000 owed.	(4) Account Payable	8,000
		Cash	8,000
5.	Pay for one year insurance policy, $600 in cash.	(6) Prepaid Insurance	600
		Cash	600
6.	Issue 10,000 shares for $100,000.	(7) Cash	100,000
		Common stock	100,000

Double-entry Accounting

❑ **From journal entries to T-accounts**

1.	Cash	100,000	
	Notes Payable		100,000
2.	Equipment	60,000	
	Cash		60,000
3.	Inventory	15,000	
	Account Payable		15,000
4.	Account Payable	8,000	
	Cash		8,000
5.	Prepaid Insurance	600	
	Cash		600
6.	Cash	100,000	
	Common stock		100,000

Cash

(1) 100	
	(2) 60
	(4) 8
	(5) 0.6
(6) 100	

Equipment

(2) 60	

Inventory

(3) 15	

Prepaid Insurance (A)

(5) 0.6	

Notes Payable

	(1) 100

Accounts Payable (L)

(4) 8	(3) 15

Common Stock (SE)

	(6) 100

❑ **The accounting process so far**

1. Analyze the transaction

2. Record the debits and credits (journal entries)

3. Post journal entries to ledger (T-accounts) ➔ aggregate the accounts (end balance)

❑ **Rules of Debits and Credits**

➢ Every transaction affects (at least) two accounts.

➢ Every journal entry must have at least one debit and at least one credit.

➢ No negative numbers are allowed. An account either has a positive debit balance or a positive credit balance.

➢ Debits = credits for every transaction

➢ Debits = credits maintains the balance sheet equation, A = L + SE.

THANK YOU!