What is Accounting?

The system in which the financial transactions of an organization for a particular period are recorded to know the operating results and the financial position of that concern to analyze and communicate the same to interested users is called Accounting.

Accounting is an information system that identifies, records and communicates the economic events of an organization to interested users.

According to the American Institute of Certified Public Accountants (AICPA): "Accounting is the art of recording, classifying and summarizing in a significant manner and in terms of money transactions and events, which are in part at least of a financial character and interpreting the results there of. "

AAA (American Accounting Association)- "The process of identifying, measuring and communicating economic information to permit to inform judgment and by decision by the uses of the information."

Book Keeping Vs. Accounting

The art of recording of all financial transactions supported valid documents in a particular method is called Book keeping .On the other hand Accounting is the task of preparing financial statements with the help of ledger balances and analyzing and interpreting the financial statements and also communicating the information to the users.

Book keeping usually involves only the recording of economic events. On the other hand accounting is a comprehensive concept that implies the entire process of identifying, Recording and communicating economic events.

Book-keeping is the primary stage of the whole accounting process. In this stage Journalizing, recording & balancing are made. On the other hand, Accounting is the second stage or final stage of whole the accounting process. In this stage financial statements are prepared with a view to find out financial results and exhibiting financial positions.

<u>Accounting is called the language of business</u>:

Accounting is called the language of business because the result of account process or accounting cycle such as journalizing, measure, trial balance, financial statement, various accounting ratios, communicating essential information about a business to concern individuals and whole of the organization.

Accounting & Its Business Decision

Characteristic of Accounting:

1. Social subject
2. Specific accounting system
3. Double entry
4. Money measurement
5. Accounting is a science
6. Information published
7. Determination of profit and loss
8. Determination of actual financial position
9. Budget preparation;
10. Purchase or sales policy
11. Production system
12. Planning
13. Ability to profit earn
14. Managerial experience determination
15. Performance evaluation
16. Total cost determination

Necessity of Accounting:

1. Fixed accounting maintained
2. Determination of profit and loss
3. Evaluation of financial condition
4. Proof certification
5. Comparative description in money transaction
6. Future planning published
7. Determination of tax
8. Loan receipt
9. Utilization of financial data
10. Determination of total debtors and creditors
11. Determination of cost
12. Historical flow chart

Accounting is aid to management or accounting helps the management:

A. Planning
B. Organizing
C. Motivating
D. Coordinating
E. Controlling
F. Preparing financial statement
G. Help to communicate with external parties
H. Budgeting
I. Giving professional advice

Users of the accounting information:

Accounting & Its Business Decision

The users are f accounting information can divided into three groups:

1. Those who manage the business – Manager
    - Owners
    - Board of directors
    - Managers
    - Department heads
    - Supervisors
    - Officers
    - Staff
2. Those outside the business who have directly interest in the business:
    - Present or potential investors
    - Present or potential creditors
3. Those persons, groups or agencies that have indirect financial interest in the business:
    - Taxing authority - State, municipals, others
    - Regular agencies – SEC, stock exchange, others
    - Economic planner- Council of economic advisors, government planners
    - Other group or unions – Employees union, labor union, financial union, customers, general public

Accounting cycle:

The orders or sequences in which accounting procedures are performed is known as accounting cycle. As soon as transaction takes place they are recorded in journal and so the accounting cycle or accounting process are begin with the journalizing and concludes with the post closing trial balance.

The Sequence of Accounting Function:

Observe events

↓

Identify economic events

↓

Measure economic events in financial terms

↓

Record measurements - Journalizing

↓

Classify measurements – Ledger

↓

Summarizing measurements – Trial balance

↓

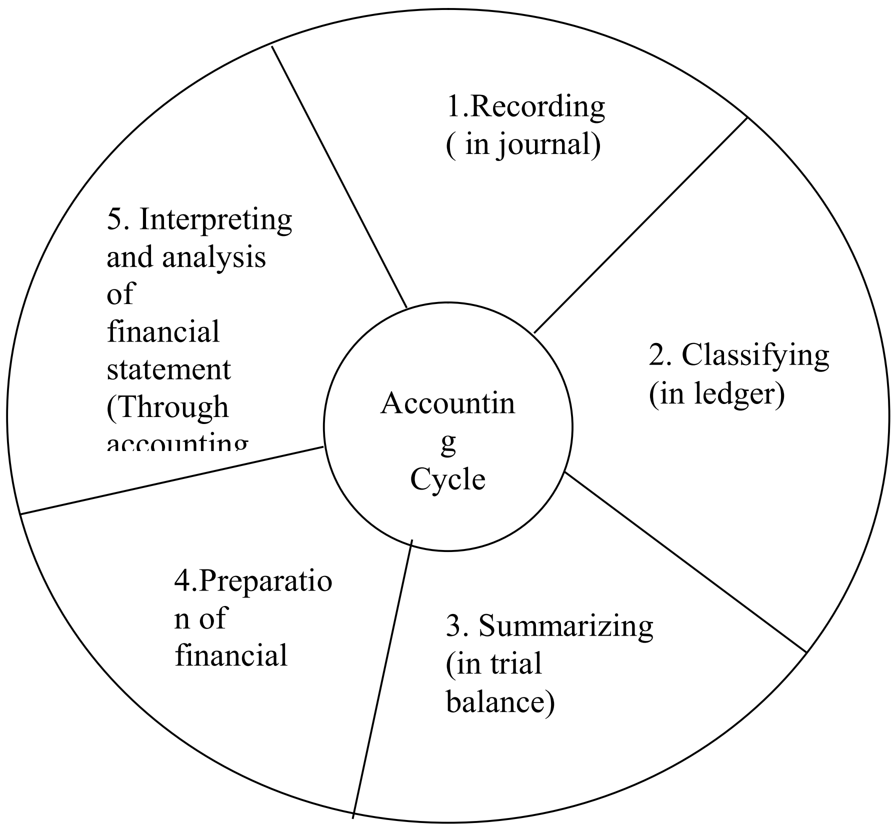
Reports economic events in financial statements and other reports

↓

Interpret the contents of financial statements and other reports.

The sequence of above function is called accounting cycle or accounting process.

Diagrammatically the accounting cycle can be shown below:



Accounting cycle consists of five steps:

1. Recording business transaction:

The first step of accounting is the recording business transaction. If any business transaction occurs it should be recorded in the journal books according to the dates chronologically. Journal is the book containing a record of each day transactions.

2. Classifying of business transaction:

Primarily the business transaction are recorded in journal book, then the transaction can be classified and posted to the ledger. Ledger is the permanent storehouse of all accounts \ transaction.

3. Summarizing transaction:

In this step preparation of trial balance. Preparing a trial balance from the debit and credit balances of ledger accounts. The main purpose of the trial balance is to taste the arithmetical accuracy of the book. The proof of the equality of the debit and credit balance is known as trial balance.

4. Preparing of financial statement:

In this step necessity adjustment maintained to prepare the trading account, profit and loss account and balance sheet. Trading account shows the gross profit or gross loss, profit account and loss account shows the net profit and net loss and balance sheet shows the overall financial position of the company.

5. Interpretation and analysis of financial statement:

Giving requisite to the interested group by calculating various accounting ratios and by interpreting the performance of the company concerned. In this step we know the financial solvency ability to profit earn and management experience of the company.

Main Forms of Business Organizations

- Single Proprietorship
- Partnership
- Corporation

Type of Business Activities of Organizations

- Service Companies- accounting firms, law firms, universities, hospitals, etc.
- Merchandising Companies-super markets, clothing stores, dealership etc.
- Manufacturing Companies-steel mills, auto manufacturers etc.

Major Financial Statements

- Income Statement- shows the performance of a specific period
- Balance Sheet- shows the financial position on a specific date
- Statement of Owners' Equity-shows the causes of change in owners' equity.
- Cash Flow Statement- shows the cash inflows and outflows of a specific period

Basic Accounting Equation

Accounting & Its Business Decision

The relationship between asset, liabilities and owners equities is called the fundamental accounting equation.

The American accountants have derived the rules of debit and credit or double entry system through the accounting equation, which is given below –

Assets = Equities

Equities may be divided into equity of creditors representing debt of the business known as liabilities and equity of the owners known as capital, keeping in view of two types of equities, the equation given below-

$$\text{Assets} = \text{Liabilities} + \text{Owners Equities}$$

$$A = L + P \text{ (proprietorship)}$$

$$A = L + O/E$$

$$A = L + C \text{ (capital)}$$

GAAP:

Accounting is the language of business. To make the language convey the same meaning to all people, accounts all over the world have developed certain rules, procedures and convention. It represents a consensus view by the professions of good accounting practices and procedures. These rules, procedures and conversion are called GAAP.

In our country, GAAP means those principal which are adopted by the ICAB (*Institute of Chartered Accountants of Bangladesh*). To any principal ICAB always remember the local, socio economic environment i.e. company law, SEC (*Security and Exchange Commission*) regulation, taxation regulation etc. Therefore which principals are regulated by the professional bodies are called the GAAP in our country.

Accounting

The Purpose of Accounting

Owners

Information Needed: Company's profitability and current financial condition.
Decisions made: If business is good, owners may consider making additional investments for growth. If business is poor, they may want to talk to management to find out why and may consider closing the business.

Managers

Information Needed: Detailed measures of business performance.
Decisions made: Managers need to make operating decisions. How much and what kinds of

inventory should be carried? Is business strong enough to support higher wages for employees?

Creditors
Information Needed: Company's profitability, debt outstanding, and assets that could be used to secure debt.
Decisions made: Should a loan be granted to this business? If so, what amount of debt can the business support and what interest rate should be charged?

Government Agencies - National, state, and local
Information Needed: Company's profitability, cash flows, and overall financial condition
Decisions made: The IRS will decide how much income tax the business must pay. Local governments may be willing to adjust property taxes paid by the business to encourage it to stay in town.

The Accounting Process
Analyzing > Recording > Classifying > Summarizing > Reporting > Interpreting

Business Ownership Structures
Sole Proprietorship (One owner)
Partnership (More than one owner)
Corporation (Owned by stockholders or shareholders)

Business Types
Services (Travel Agency, Computer Consultant, Physicians)
Merchandising (Department Store, Pharmacy, Jewelry Store)
Manufacturing (Automobile Manufacturer, Furniture Maker, Toy Factory)

Accounting Elements

Business Entity - An individual, association, or organization that engages in economic activities and controls specific economic resources.

Three basic accounting elements - Assets, Liabilities, and Owner's Equity

Assets are items that are owned by a business and will provide future benefits. Examples of assets include cash, merchandise, furniture, fixtures, machinery, buildings, and land. Businesses may also have an asset called accounts receivable.

Liabilities represent something owed to another business entity. The amount owed represents a probable future outflow of assets as a result of a past event or transaction. The most common liabilities are accounts payable which is an unwritten promise to pay a supplier for assets purchased or services received.

Owner's equity is the amount by which the business assets exceed the business liabilities. Other terms used for owner's equity include net worth and capital.

The accounting equation

Accounting & Its Business Decision

Assets = Liabilities + Owner's Equity

Liabilities represent the outside interests of creditors, Owner's equity represents the inside interests of owners.

Analyzing Business Transactions

A business transaction is an economic event that has a direct impact on the business. A business transaction almost always requires an exchange between the business and another outside entity. Examples of business transactions include buying goods and services, selling goods and services, buying and selling assets, making loans, and borrowing money. All business transactions affect the accounting equation through specific accounts. An account is a separate record used to summarize changes in each asset, liability, and owner's equity of a business. Account titles provide a description of the particular type of asset, liability, or owner's equity affected by a transaction.

Revenues represent the amount a business charges customers for products sold or services performed. Separate accounts are used to recognize different types of revenue. Examples include Delivery Fees: Consulting Fees: Rent Revenue, if the business rents space to others: Interest Revenue, for interest earned on bank deposits; and Sales, for sales of merchandise. *Revenues increase both assets and owner's equity.*

Expenses represent the decrease in assets (or increase in liabilities) as a result of efforts made to produce revenues. Common examples of expenses are rent, salaries, supplies consumed, and taxes. Separate accounts are used to maintain records for each different type of expense. Expenses are "incurred" as assets are consumed (such as supplies), cash is paid for services performed for the business, or a promise is made to pay cash at a future date for services performed for the business (such as wages). *Expenses either decrease assets or increase liabilities.*

Net income or net profit for the period is when total revenues exceed total expenses of the period.
Revenues Greater than Expenses = Net Income

Net loss for the period is when expenses exceed revenues of the period.
Expenses Greater than Revenues = Net Loss

Any accounting period of twelve months is called a fiscal year and frequently coincides with the calendar year.

Withdrawals, or drawing reduce owner's equity as a result of the owner taking cash or other assets out of the business for personal use.

Example Transactions

Transaction: Investment by owner
An Increase in an Asset Offset by an Increase in Owner's Equity.

Accounting & Its Business Decision

Transaction:: Purchase of an asset for cash.
An Increase in an Asset Offset by a Decrease in Another Asset.

Transaction: Purchase of an asset on account
An Increase in an Asset Offset by an Increase in a Liability.

Transaction: Payment on a loan
A Decrease in an Asset Offset by a Decrease in a Liability.

Transaction: Delivery revenues earned in cash
An Increase in an Asset Offset by an Increase in Owner's Equity Resulting from Revenue.

Transaction: Paid rent for month
A Decrease in an Asset Offset by a Decrease in Owner's Equity Resulting from an Expense.

Transaction: Paid telephone bill
A Decrease in an Asset Offset by a Decrease in Owner's Equity Resulting from an Expense.

Transaction: Delivery revenues earned on account
An Increase in an Asset Offset by an Increase in Owner's Equity Resulting from Revenue.

Transaction: Purchase of supplies
An Increase in an Asset Offset by a Decrease in an Asset.

Transaction: Payment of insurance premium
An Increase in an Asset Offset by a Decrease in an Asset.

Transaction: Cash receipts from prior sales on account
An Increase in an Asset Offset by a Decrease in an Asset.

Transaction: Purchase of an asset on account making a partial payment
An Increase in an Asset Offset by a Decrease in an Asset and an Increase in a Liability

Transaction: Payment of Wages
A Decrease in an Asset Offset by a Decrease in Owner's Equity Resulting from an Expense.

Transaction: Deliveries made for cash and on account
An Increase in Two Assets Offset by an Increase in Owner's Equity.

Transaction: Withdrawal of cash from business
A Decrease in an Asset Offset by a Decrease in Owner's Equity Resulting from a Withdrawal by the Owner.

Financial Statements

The Income Statement, sometimes called the profit and loss statement or operating statement, reports the profitability of business operations for a specific period of time.

The Statement of Owner's Equity reports on these activities for a specific period of time.

Accounting & Its Business Decision

The Balance Sheet reports a firm's asset's, liabilities, and owner's equity on a specific date. It is also referred to as a statement of financial position or statement of financial condition.

Accounting Process Overview

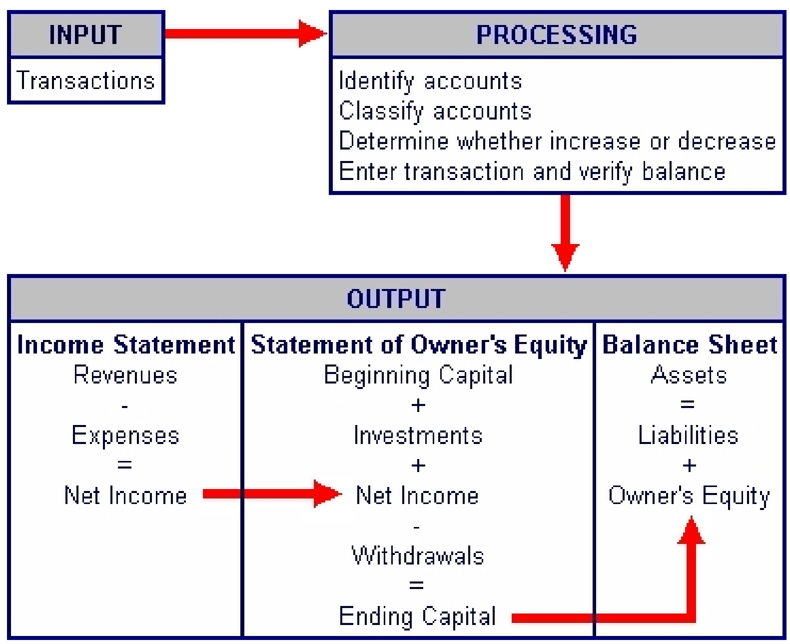
There are three basic phases of the accounting process in terms of input, processing, and output.

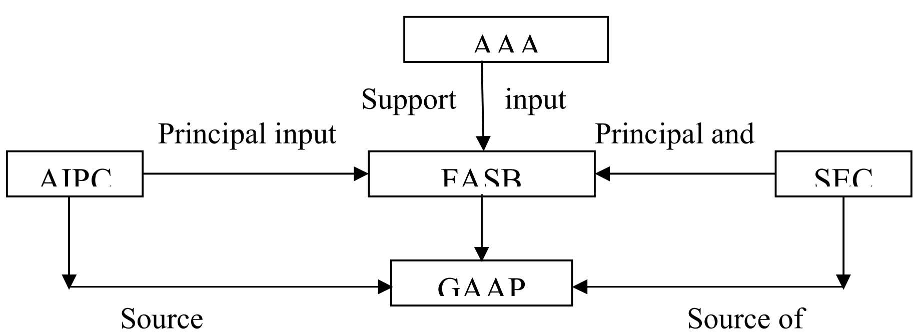
Input. Business transaction provide the necessary input.

Processing. Recognizing the effect of these transactions on the assets, liabilities, owner's equity, revenues, and expenses of a business is the processing function.

Output. The financial statements are the output.

Flow Chart





Accounting & Its Business Decision

AAA= American Accounting Association
AIPCA=American Institute of Certified Public Accounts
FASB=Financial Accounting Standard Board
SEC=Securities and Exchange Commission
GAAP=Generally Accepted Accounting Principals

Double entry accounting or system:
Each business transaction effects the accounting element in at least two ways, recording both effects of a transaction is called double entry accounting or system. The double entry system provides a means of verifying the arithmetical accuracy of both transactions. When both effects of a transaction have been recorded, assets=Liability + Owner Equity. In other words an accounting system that involve recording the effects of each transaction as debit and credit.

Rules of double entry system or rules of debit and credit:

Dr Any assets a/c Cr

(+) Increase side (Normal bal.)	(-) Decrease side

Dr Any expense a/c Cr

(+) Increase side (Normal bal.)	(-) Decrease side

Dr Any withdrawing a/c Cr

(+) Increase side (Normal bal.)	(-) Decrease side

Dr Any liabilities a/c Cr

(-) Decrease side	(+) Increase side (Normal bal.)

Dr Capital a/c Cr

(-) Decrease side	(+) Increase side (Normal bal.)

Dr Income/profit/gain a/c Cr

(-) Decrease side	(+) Increase side (Normal bal.)

Accounts: Written documents or written records of a business, assets, liabilities and owners equities are called an account. In other words an account is simply a place where similar transactions and events, which are occurred during a particular period of time, are recorded, summarized and accumulated.

Each account has debit on the left side and credit on the right side. An account contain the following information:

1. Name of Account Ex-Building, rent, machinery, cash, etc.

2. Folio Number: This is the page number of the book in which account appear.
3. Date: The date of recording information in the account.
4. Particulars: This is actually the name of opposite account involved in the transactions recorded in the account.
5. Journal Folio: This is the page number of the journal from where posting is made.
6. Amount: This is the amount of the entry.

The main idea of accounting is that the sum of claims of an organization (assets) must always be equal to the sum of claim to an organization (liabilities) i.e.

Assets = Liabilities + Owner's Equity

Assets: Resources owned by a business e.g. cash, property, machinery, debtor, investment, expense paid in advance etc.

Liabilities: The claims against the assets other than that of owners e.g. loan, creditors, note payable, unpaid expense etc.

Owner's Equity:

The ownership claim against the total assets e.g. investment by owner, share of profit retained in business etc. It is simply the difference between the assets and liabilities.

Few transactions that increase/decrease these three components:

SL	Increases Assets	Decreases Assets
1	Cash Sale	Buy assets on cash
2	Investment by owner	Payment to creditors
3	Sale on credit	Depreciation of an asset
4	Prepaid expense	Pay for an expense by bank
5	Buy an equipment	Sale of an asset

SL	Increases Liabilities	Decreases Liabilities
1	Buy goods on credit	Payment due expense
2	Take loan	Payment of note payable
3	Bank overdraft	Payment to creditors
4	Buy asset on note payable	Paid for tax liabilities
5	Received cash but service will be provided in future	Get discount while paying to creditors

Accounting & Its Business Decision

SL	Increases owner's equity	Decreases owner's equity
1	Investment in business	Withdraw from business
2	Revenue of business	Expense of business
3	Profit of business	Loss of business

Practical Problem:1

Mr Jhon opens his accounting office on august1, 2003. During the first month of the operations, the following transactions occurred.

Aug-1: Invested 1,00, 0000 Tk. in cash in accounting practice.

Aug-3: Paid 7,500 Tk. for August rent of the office space

Aug-5: Purchased office equipment on account 32,000Tk.

Aug-8: Received from clients 10,000Tk. in advance for service

Aug-15: Borrowed 18,000Tk. by issuing a note.

Aug-17: Payment the full bill of equipment purchased

Aug-20: Performed full service for advance received from customer

Aug-24: Performed services for clients of 30,000Tk.and received 60% of it in cash.

Aug-31: Paid for monthly expenses: salaries 12,000 and utilities 5,000.

Requirements:

1. Prepare summery of transaction showing the effects in equation for the above transactions.
2. Prepare Income statement, owner's equity statement and balance sheet at August 31 for Mr. Jhon & co.

Practical Problem:2

Cindy Craford started his own delivery service, Cindy Craford deliveries, on June 1, 2001. The following transactions occurred during the month of June.

June 1, Cindy Craford invested $4,00,000 cash in business.
June 5, Purchased a used van for deliveries for $30,000. Cindy Craford paid $6,000 cash and signed a notes payable for the remaining balance.
June 10, Paid $950 for office rent for the month.
June 14, Purchased office supplies for $850 on account.
June 15, Paid $450 for utilities.
June 18, Paid $900 for employees salaries.
June 20, Borrowed $7,000 from the bank.

June 21, Purchase office equipment $50,000; paying 10,000 in cash and the balances are on account.
June 23, Earned revenues of $74,000 of which $20,000 is collected in cash and the balances are due.
June 25, Withdrew $1000 in cash for personal use.
June 28, The payment of 50% of the notes payable in transaction June 5
June 30, The collection of 20% of accounts receivable in the transaction June28.

Requirements:

a) Record Cindy Craford June transactions in an expanded accounting equation .Use the description column to provide a brief explanation of each transaction.
b) Prove the Accounting Equation.

Practical Problem:3

Michelle Pleiffer started his own delivery service, Michelle Pleiffer deliveries, on June 1, 2001. The following transactions occurred during the month of June.

1. Michelle Pleiffer invested $3,00,000 cash and accounts receivable $2,00,000 in business.
2. Purchased a used machinery for $60,000. Michelle Pleiffer paid $10,000 cash and signed a notes payable for the remaining balance.
3. Paid $100 for office rent for the month.
4. Purchased office supplies for $800 on account.
5. Paid $650 for utilities.
6. Paid $2,000 for employees salaries.
7. Borrowed $10,000 from the bank.
8. Purchase office equipment $70,000; paying 10,000 in cash and the balances are on account.
9. Earned revenues of $74,000 of which $20,000 is collected in cash and the balances are due.
10. Withdrew $2,000 in cash for personal use.
11. The payment of 20% of the notes payable in transaction no.(2)
12. The collection of 30% of accounts receivable in the transaction no.(9)

Requirements:

a. Record Michelle Pleiffer June transactions in an expanded accounting equation .Use the description column to provide a brief explanation of each transaction.
b. Prove the Accounting Equation.

Practical Problem:4

Ron Salem started his own delivery service, Salem deliveries, on July 1, 2003. The following transactions occurred during the month of July.

July 1, Ron invested $20,000 cash in business.
July 5, Purchased a used van for deliveries for $20,000. Ron paid $4,000 cash and signed a notes payable for the remaining balance.
July 10, Paid $1,000 for office rent for the month.
July 14, Purchased office supplies for $300 on account.

July 15, Paid $500 for utilities.
July18, Paid $1,000for employees salaries.
July 20, Performed $8,000 of service on account.
June 21, Received a cash payment of $1,500 for service provided on July 20.
July 23, Purchased office supplies for200 on account.
July 25, Withdrew $400 in cash for personal use.
July 26, Paid for the office supplies purchased on account on July23.
July 28, Received a cash payment of $3,000 for service provided
July 30,Make a cash payment of $1,000 on the notes payable.

Requirements:

c) Record Ron Salem July transactions in an expanded accounting equation .Use the description column to provide a brief explanation of each transaction.
d) Prove the Accounting Equation.

Practical Problem:5

Yanni company started his own consulting firm, Yanni consulting, on May1, 2002. The following transactions occurred during the month of May.

May 1, Yanni invested $8,00,000 cash in the business.
May 8, Purchased a used machinery for $60,000. Yanni paid $10,000 cash and signed a notes payable for the remaining balance.
May 10, Paid $100 for office rent for the month.
May 12, Purchased office supplies for $800 on account.
May 13, Paid $650 for utilities.
May 16, Paid $2,000 for employees salaries.
May 19, Borrowed $10,000 from the bank.
May 21, Purchase office equipment $70,000; paying 10,000 in cash and the balances are on account.
May 22, Earned revenues of $74,000 of which $20,000 is collected in cash and the balances are due.
May 26, Withdrew $2,000 in cash for personal use.
May 29, The payment of 20% of the notes payable in transaction May 8
May 30, The collection of 30% of accounts receivable in the transaction May 22.

Requirements:

a. Record Yanni May transactions in an expanded accounting equation .Use the description column to provide a brief explanation of each transaction.
b. Prove the Accounting Equation.

Practical Problem:6

Medco started his own delivery service, Medco deliveries, on January 1, 2000. The following transactions occurred during the month of January.

January 1: Medco invested $30,000 cash in the business.
January 1: Purchased a old van for deliveries for $15,000 for the purpose of deliveries. Medco paid $5,000 cash and signed a notes payable for $10,000.
January 3 : Paid cash $1,000 for office rent for the month of January 2003.

January 7 : Purchased office supplies for cash $1,000.
January 10 : Paid electric bill $500.
January 12 : Paid salary of staff for the month $2,000.
January 13 : Borrowed $17,000 from the bank.
January 17 : Purchase a delivery van for $20,000 on account.
January 21 : Earned revenues of $11,000 of which $3,000 is collected in cash and the balances are due.
January 24 : Withdrew cash $1,000 from the business for personal use.
January 27, Paid $3,500 bills for advertisement.
January 29 : Purchased supplies for cash $1,000
January 30: Cash received $2,000 for service of January 21

Requirements:

a. Show the effects of the transactions on the accounting equation using the following format:

Assets ==Liabilities + Owner's Equity
Date Cash + Accounts Receivable + supplies+ D. Van = Accounts payable+ Notes payable + Capital

b. Prepare an Income Statement;
c. Prepare a statement of owner's equity;
d. Prepare a Classified Balance Sheet in an account form.

Short Problems

1. Balance of total assets of AIUB on January 1, 2002 was Tk. 90,000,000 and total liabilities Tk. 40,000,000. If assets increased by 10% and owner's equity decreased by 15% during the year, what is the amount of total liabilities on December 31, 2002.
2. If at the beginning of a year amount of owner's equity of a business is Tk. 100,000. During the year there was an additional investment by the owner of Tk. 50,000 and no withdrawal. At the end of the year total amount of assets and liabilities was Tk.470, 000 and Tk. 300,000 respectively. Determine the amount of net income/ loss of the business during the year.
3. In addition to the data of question no. 2, if there was also a withdrawal of Tk. 25,000 in that year what would be the amount of net income/loss during the year?

PROBLEM 7

The following financial statement information is known about five separate proprietorships:

	Company A	**Company B**	**Company C**	**Company D**	**Company E**
December 31, 2001:					
Assets	$66,000	$28,500	$89,000	$70,000	**?**
Liabilities	32,000	22,500	40,000	35,000	$20,000
December 31, 2002:					
Assets	**?**	30,000	91,000	66,000	60,000

Liabilities	28,000	23,000	**?**	41,000	15,000
During year 2002:					
Owner investments	2,000	3,000	- 0 -	3000	5,000
Net income (loss)	15,000	**?**	(7,000)	**?**	20,000
Owner withdrawals	8,000	5,500	3,000	2,000	10,000

Required

1. Answer the following questions about Company A:
  a. What is the equity amount on December 31, 2001?
  b. What is the equity amount on December 31, 2002?
  c. What is the amount of assets on December 31, 2002?
2. Answer the following questions about Company B:
  a. What is the equity amount on December 31, 2001?
  b. What is the equity amount on December 31, 2002?
  c. What is net income (loss) for year 2002?
3. Calculate the amount of liabilities for Company C on December 31, 2002.
4. Calculate the amount of income (loss) for Company D during year 2002.
5. Calculate the amount of assets for Company E on December 31, 2001.

PROBLEM 8

Identify how each of the following separate transactions affects financial statements. For the balance sheet, identify how each transaction affects total assets, total liabilities, and equity. For the income statement, identify how each transaction affects net income. For the statement of cash flows, identify how each transaction affects cash flows from operating activities, cash flows from financing activities, and cash flows from investing activities. For increases, place a "+" in the column or columns. For decreases, place a "-" in the column or columns. If both an increase and a decrease occur, place a "+/-" in the column or columns. The first transaction is completed as an example.

		Balance Sheet			**Income Statement**	**Statement of Cash Flows**		
	Transaction	**Total Assets**	**Total Liab.**	**Equity**	**Net Income**	**Operating Activities**	**Financing Activities**	**Investing Activities**
1	Owner invests cash	+		+				
+								
2	Buys supplies for cash							
3	Buys supplies on credit							

4	Pays rent with cash
5	Perform services on credit
6	Pays cash on payable from (3)
7	Owner withdraws cash
8	Performs services for cash
9	Collects cash on receivable from (5)
10	Ordered supplies

PROBLEM 9 :A software company, Herds-of-Nerds, has the following beginning cash balance and cash flows for the month of April:

Cash balance, April 1	$ 0
Cash withdrawal by owner	1,000
Cash received from customers	6,000
Repayment of debt	2,500
Cash paid for store supplies	1,600
Cash purchase of computers	18,000
Cash paid for utilities	3,000
Cash paid to employees	3,300
Cash investment by owner	25,000

Required

Prepare a statement of cash flows for Herds-of-Nerds for the month of April.

PROBLEM 10 : Martin Mark, an amatuer magician started a new business called Martin's Magnificent Magic and completed the following transactions during his first month of operations:

a. Mark invests $3,000 cash and magic supplies valued at $1,500 in the business.

b. Purchased $2,000 of additional magic supplies on credit.

c. Paid $500 for advertising on local radio station.

d. Performed show at wedding and collected $800 cash.

e. Puchased a used mini-van for $4,500. Mark paid $1,000 and signed a note payable for the remainder.

f. Gave magic show at local school and billed school $1,200 for show.

g. Paid seamtress $40 to repair ripped coat pocket from child who tried to find the disappearing card.

h. Mark withdrew $100 to pay personal expenses.

i. Received $1,200 cash from the client described in transaction *f.*

j. Paid for supplies purchased in transaction *b.*

k. Paid $80 monthly fee to answering service..

Required

Preparation Component

1. Create a table, using the following headings for the columns: Cash; Accounts Receivable; Supplies; Vehicle; Accounts Payable; Note Payable; and M Mark, Capital. Leave space for an Explanation column to the right of the Capital column. Identify revenues and expenses by name in the Explanation column.

2. Use additions and subtractions to show the transactions' effects on individual items of the accounting equation. Show new balances after each transaction. Indicate next to each change in equity whether it was caused by an investment, a revenue, an expense, or a withdrawal.

3. Once you have completed the table, determine the company's net income.

Analysis Component

4. Determine the return on equity for Martin's Magnificent Magic (use the $4,500 initial investment as the beginning balance of equity). Assuming Mark could have earned $1,000 for the period from another job, determine the modified return on equity for the period. State whether you think the business is a good use of Mark's money if an alternative investment would have returned 7% for the same period.

PROBLEM 10

Tired of flipping burgers for a living, local headbahnger Sheila Sham forms her own band, Sheila and The Screamers. The band began operations on May 1 and completed the following transactions during the month:

May 1 Sheila invested $10,000 cash in the business.
1 Purchased $2,500 of audio equipment with cash.
3 Rented a garage to rehearse and paid $200 for a month's rent.
5 Billed local college $1,000 for first performance.
8 Paid bass player's and drummer's wages of $300.
12 Played next gig at biker convention and collected $2,000 cash.
15 NOT LOUD ENOUGH! Purchased another $5,000 audio equipment paying $2,000
cash with remainder due in 30 days.
20 Purchased $100 of earplugs on credit to distribute to neighbors (PR expense).
22 Collected cash from school billed on May 5.
28 Paid for earplugs purchased on May 20.
29 Perfomed show at local pub and collected $1,500.
30 Paid pub $200 to cover damage by bikers who crashed the show.
30 Paid bass player's and drummer's wages of $300.
30 Purchased additional audio equipment on credit for $400.
30 In order to convince banker U. O. Lotz to lend them money to record a CD, the band
plays a song in his office. Mr. Lotz agrees to lend the money if they will stop playing immediately! Sheila borrows $20,000 and receives cash from the bank (record as Accounts Payable).
30 Performed another gig at local pub on credit and billed pub $1,500.
30 Sheila withdrew $500 cash from the business for personal use.

Required

1. Arrange the following asset, liability, and equity titles in a table like Exhibit 2.13: Cash; Accounts Receivable; Prepaid Insurance; Equipment; Accounts Payable; Notes Payable and Sham, Capital. Include an Explanation column for changes in equity.

2. Show effects of the transactions on the items of the accounting equation by recording increases and decreases in the appropriate columns. Do not determine new account balances after each transaction. Next to each change in equity, state whether it was caused by an investment, a revenue, an expense, or a withdrawal. Determine the final total for each item and verify that the equation is in balance.

3. Prepare an income statement for May, a statement of changes in owner's equity for May, a May 31 balance sheet, and a statement of cash flows for May.

PROBLEM 11

The accounting records of Blues Tunes Music Company show the following assets and liabilities as of December 31, 2001, and 2002:

	December 31	
	2001	**2002**
Cash	$72,000	$28,500
Accounts receivable	25,000	24,000
Office supplies	4,500	2,000
Office equipment	129,000	125,000
Trucks	23,000	23,000
Building	0	90,000
Land	0	50,000
Accounts payable	8,700	24,400
Note payable	0	60,000

Late in December 2002, Ken Sheppard, the owner, purchased a small office building and moved the business from rented quarters to the new building. The building and the land it occupies cost $140,000. The business paid $80,000 cash toward the purchase and a $60,000 note payable was signed for the balance. Sheppard had to invest $20,000 cash in the business to enable it to pay the $80,000. Sheppard also withdraws $2,000 cash per month from his proprietorship for personal expenses.

Required

1. Prepare balance sheets for the business as of December 31, 2001, and 2002. (Remember that equity equals the difference between assets and liabilities.)

2. By comparing equity amounts from the balance sheets and using the additional information presented in this problem, prepare a calculation to show how much net income was earned by the business during 2002.

3. Calculate the year 2002 return on equity for the business. Also calculate the modified return on equity assuming that Sheppard's efforts are worth $33,000 for the year.

PROBLEM 12

Jerome Garcia started a new business and completed these transactions during August:

Aug. 1 Garcia transferred $48,000 cash from a personal savings account to a checking account in the name of Garcia Space Exploration.

1 Rented office space and paid $800 cash for the August rent.

3 Purchased exploration equipment for $22,000 by paying $12,000 cash and agreeing to pay the balance in 3 months.

5 Purchased office supplies by paying $1,500 cash.

6 Completed exploration work and immediately collected $420 cash for the work.

8 Purchased $1,350 of office equipment on credit.

15 Completed exploration work on credit in the amount of $8,000.

18 Purchased $700 of office supplies on credit.

20 Paid cash for the office equipment purchased on August 8.

24 Billed a client $2,400 for work completed; the balance is due in 30 days.

28 Received $5,000 cash for the work completed on August 15.

30 Paid the assistant's salary of $1,100 cash for this month.

30 Paid $340 cash for this month's utility bill.

30 Garcia withdrew $1,050 cash from the business for personal use.

Required

Preparation Component

1. Arrange the following asset, liability, and equity titles in a table like Exhibit 2.13: Cash; Accounts Receivable; Office Supplies; Office Equipment; Exploration Equipment; Accounts Payable; and Jerome Garcia, Capital. Leave space for an Explanation column to the right of Garcia, Capital.

2. Use additions and subtractions to show the effects of each transaction on the items in the accounting equation. Show new balances after each transaction. Next to each change in equity, state whether the change was caused by an investment, a revenue, an expense, or a withdrawal.

3. Use the increases and decreases in the last column of the table from part 2 to prepare an income statement and a statement of changes in owner's equity for the month. Also prepare a balance sheet as of the end of the month.

4. Calculate the return on equity for the month, using the $48,000 initial investment as the beginning balance of equity.

Analysis Component

5. Assume the investment transaction on August 1 was \$30,000 instead of \$48,000 and that Hamilton obtained the \$18,000 difference by borrowing it from a bank. Explain the effect of this change on total assets, total liabilities, equity, and return on equity.