



Presents

Introduction to Accounting-Basics of Accounting and Financial Statements

Areas to be covered:

- Golden Rule of Accounting:
 - Personal Account:
(Debit the Receiver, Credit the Giver)
 - Real Account:
(Debit what comes in, Credit what goes Out)
 - Nominal Account:
(Debit all Expenses and Losses, Credit all Income and Gains)
- Introduction to Financial Statements
 - Balance Sheet (Comprise of Assets & Liabilities)
 - Profit & Loss Statement (Gross Profit & Net Profit)
 - Statement of Cash Flows/ Cash Flow Statement
(Operating Activities, Investment Activities, Financing Activities)

1. GOLDEN RULES OF ACCOUNTING:

a. Personal Account: (Debit the Receiver, Credit the Giver)

These accounts are related to individuals, firms, companies, etc. A few examples of personal accounts include debtors, creditors, banks, outstanding/prepaid accounts, accounts of credit customers, accounts of goods suppliers, capital, drawings, etc.

Natural personal accounts:

This type of personal accounts is the simplest to understand out of all and includes all god's creations who have the ability to deal, who, in most cases, are people. E.g. Kumar's A/C, Ram's A/C, etc.

Artificial personal accounts:

Personal accounts which are created artificially by law, such as corporate bodies and institutions, are called Artificial personal accounts. E.g. Pvt Ltd companies, LLCs, LLPs, clubs, schools, etc.

Representative personal accounts:

Accounts which represent a certain person or a group directly or indirectly. E.g. Let's say that wages are paid in advance to an employee – a wage prepaid account will be opened in the books of accounts. This wage prepaid account is a representative personal account indirectly linked to the person.

b. Real Account: (Debit the receiver, Credit the Giver)

All assets of a firm, which are tangible or intangible, fall under the category "Real Accounts"

Tangible real accounts:

They are related to things that can be touched and felt physically. A few examples of tangible real accounts are building, machinery, stock, land, etc.

Intangible real accounts:

They are related to things that can't be touched and felt physically. A few examples of such real accounts are goodwill, patents, trademarks, etc.

c. Nominal Account: (Debit all Expenses & Losses, Credit all Income and Gains)

Accounts which are related to expenses, losses, incomes or gains are called Nominal accounts. Nominal accounts do not really exist in physical form, but behind every nominal account money is involved. E.g. Purchase A/C, Salary A/C, Sales A/C, Commission received A/C, etc.

The final result of all nominal accounts is either profit or loss which is then transferred to the capital account.

INTRODUCTION TO FINANCIAL STATEMENTS:

- **Balance Sheet:** A balance sheet is a financial statement that summarizes a company's assets, liabilities and shareholder's equity at a specific point in time. These three balance sheet segments give investors an idea as to what the company owns and owes, as well as the amount invested by shareholders.

The balance sheet adheres to the following formula:

Assets (Dr.) = Liabilities (Cr.) + Shareholders' Equity (Cr.)

ASSETS: (Debit Balances)

Within the assets segment, accounts are listed from top to bottom in order of their liquidity, that is, the ease with which they can be converted into cash. They are divided into current assets, those which can be converted to cash in one year or less; and non-current or long-term

assets, which cannot.

Current Assets:

- Cash & Cash Equivalents
- Marketable Securities: Equity and debt securities for which there is a liquid market
- Accounts Receivable
- Inventory
- Prepaid Expenses

Long-Term Assets:

- Long-Term Investments: Securities that will not or cannot be liquidated in the next year
- Fixed Assets
- Intangible Assets: Example – Goodwill

LIABILITIES & SHAREHOLDER EQUITY: (*Credit Balances*)

Liabilities are the money that a company owes to outside parties, from bills it has to pay to suppliers to interest on bonds it has issued to creditors to rent, utilities and salaries. Current liabilities are those that are due within one year and are listed in order of their due date. Long-term liabilities are due at any point after one year.

Current Liabilities:

- Interest Payable
- Rent/ Tax/ Utilities Payable
- Wages Payable
- Customer Prepayments

Long-Term Liabilities:

- Long-Term Debt
- Deferred Tax Liability

Shareholder's Equity:

Shareholder's equity is the money attributable to a business's owners, meaning its shareholders. It is also known as "net assets", since it is equivalent to the total assets of a company minus its liabilities, that is, the debt it owes to non-shareholders.

- **Capital & Additional paid-in capital:** In general terms, 'capital' refers to any financial resources or assets owned by a business that are useful in furthering development and generating income.
- **Retained Earnings:** They are the net earnings a company either reinvests in the business or uses to pay off debt.

Example Company
Balance Sheet
December 31, 2016

ASSETS

Current assets	
Cash	\$ 2,100
Petty cash	100
Temporary investments	10,000
Accounts receivable - net	40,500
Inventory	31,000
Supplies	3,800
Prepaid insurance	1,500
Total current assets	<u>89,000</u>
Investments	<u>36,000</u>
Property, plant & equipment	
Land	5,500
Land improvements	6,500
Buildings	180,000
Equipment	201,000
Less: accum depreciation	<u>(56,000)</u>
Prop, plant & equip - net	<u>337,000</u>
Intangible assets	
Goodwill	105,000
Trade names	<u>200,000</u>
Total intangible assets	<u>305,000</u>
Other assets	<u>3,000</u>
Total assets	<u><u>\$ 770,000</u></u>

LIABILITIES

Current liabilities	
Notes payable	\$ 5,000
Accounts payable	35,900
Wages payable	8,500
Interest payable	2,900
Taxes payable	6,100
Warranty liability	1,100
Unearned revenues	<u>1,500</u>
Total current liabilities	<u>61,000</u>
Long-term liabilities	
Notes payable	20,000
Bonds payable	<u>400,000</u>
Total long-term liabilities	<u>420,000</u>
Total liabilities	<u>481,000</u>

STOCKHOLDERS' EQUITY

Common stock	110,000
Retained earnings	220,000
Accum other comprehensive income	9,000
Less: Treasury stock	<u>(50,000)</u>
Total stockholders' equity	<u>289,000</u>
Total liabilities & stockholders' equity	<u><u>\$ 770,000</u></u>

The notes to the sample balance sheet have been omitted.