13 THE BALANCE SHEET

Objectives

At the end of this chapter, students should be able to:

- Distinguish between assets and liabilities. Identify the different types of assets and liabilities;
- Classify assets and liabilities;
- Prepare a balance sheet;

13.1 Introduction

After the preparation of the trading, profit and loss accounts at the end of the year, the balance sheet is finally prepared to show the state of affairs of the business at a given date. The balance sheet therefore, is a statement of what a business owns (assets) and what it owes (liabilities) to other people. The balance sheets shows the debit and credit balance existing in the ledger on a particular date after the profit and loss account has been prepared.

A balance sheet is often required by investors, the public and government to assess the financial position of a business at a particular date. If a business applies for loan from a bank, its balance sheet will be demanded. In addition, the Companies Decree Act of 1990 (CAMA) requires all businesses to prepare the profit and loss account and balance sheet for various reasons including tax assessment.

13.2 Assets

Assets are those items owned by the business e.g. cash, debtors, stock, machinery and building, etc. They are those things in which the money of the business has been invested.

Assets are classified as follows:

i. Current Assets: These are also known as circulating assets or floating assets. These are made up of cash in hand, cash at bank and other items that can easily be converted into cash such as debtors, stock in hand, etc.

ii. Fixed Assets: These are items of permanent nature bought and used over a number of years in the running of the business and are therefore, subject to wear and tear called depreciation e.g. furniture and fitting, land and building, motor van, plant and machinery, etc.

13.3 Liabilities

Liabilities are the debts owed to others by the business e.g. creditors, bank overdraft, loans, etc.

Liabilities are classified as follows:

i. Current Liabilities: Current liabilities are debts owed by the business which must be settled within a short period e.g, bank overdraft and trade discount.

ii. Long-term liabilities: These are debts which could be settled over a long period of time e.g. bank loan.

Capital

This is the amount the business owes the proprietor. In accounting, a business is regarded as a separate entity from its proprietor. Therefore, the amount introduced into the business by the proprietor is the capital and is shown as a liability in the balance sheet.

13.4 Procedure for the Preparation of a Balance Sheet

A balance sheet is a statement of affairs of a business at a given time. The correct heading of a balance sheet is stated as follows: "Balance Sheet as at December 31st, 20xx."

i. A balance sheet is not an account and should not be prefixed with "Dr", 'to' or 'by'. It is a list of all the balances remaining after trading, profit and loss account have been prepared.

ii. The layout of a balance sheet can either be in the vertical form or 'T' form.

iii. In the vertical form; the list of assets given first; followed by the list of liabilities written directly below the assets.

iv. In the 'T' form, the list of assets is written on the right hand side and the list of liabilities on the left.

v. The assets and liabilities are usually arranged under heading in the order of their permanence, that is, in the order in which the liabilities will be paid off and the assets could be turned into cash.

13.4.1 Format for a Balance Sheet

Balance Sheet as at 31st December, 20xx

	₦	₦		₦	₦
Capital			Fixed Assets		
Balance	xx		Building	xx	
Add net profit	xx	xx	Plant & machinery	xx	
Long term liabilities			Fixture & Fitting	xx	xx
Loan	xx		Current Assets		
Current liabilities			Stock	xx	
Trade creditors	xx		Debtors	xx	
Bank overdraft	xx	xx	Cash at bank	xx	
			Cash in hand	xx	xx
		xx			xx

Example 13.1

The following balances have been taken from the ledgers of Oladunni and Sons Trading Enterprises: Land and building N490,000; Plant & Machinery N400,000; Motor vehicle N50,000; Furniture and Fittings N80,000; Stock N100,000;

Debtors N24,000; Bank balance N10,000; cash in hand N2,000

January 1st, capital N700,000; creditors N44,000 and Net Profit N12,000

Solution

Oladunni and Sons Trading Enterprises

Balance Sheet as at 31st December, 2003

	₦	₦		₦	₦
Capital	700,000		Fixed Asset		
Add net profit	12,000	712,000	Land & Building	490,000	
Long term liability			Plant & Machinery	400,000	
Loan		500,000	Motor vehicle	150,000	
Current Liability			Furniture & Fitting	80,000	1,120,000
			Current Assets		
Creditors		44,000	Stocks	100,000	
			Debtors	24,000	
			Bank balance	10,000	
			Cash in hand	2,000	136,000
		1,256,000			1,256,000

In preparing the balance sheet, the assets have been arranged under fixed assets and current assets in their order of permanence. The sub-total of each sub-heading has been clearly stated, for fixed and current assets respectively. The liabilities too have been grouped as capital, long term liability and current liability in their order of permanence. The above is a 'T' form of a balance sheet which can be prepared in an alternative way by arranging the assets and liabilities in vertical order as follows: Using the same illustration given above.

Oladunni and Sons Trading Enterprises

Balance Sheet as at 31st December, 2003

	₦	₦
Fixed Assets		
Land and building	490,000	
Plant and machinery	400,000	
Motor vehicle	150,000	
Furniture and Fittings	80,000	1,120,000
Current Assets		
Stock	100,000	
Debtors	24,000	
Bank balance	10,000	
Cash in hand	2,000	136,000
Less Current Liabilities		
Creditors	44,000	92,000
		1,212,000

Represented by:	
Capital	700,000
Add Net Profit	12,000
Loan	500,000
	1,212,000

(A vertical form of a balance sheet)

13.5 Summary

In this chapter, students have learnt that:

– A balance sheet is a statement showing the financial position of a business as at a given date.
– The assets of a business are those items it owns.
– Assets could be divided into fixed and current assets.
– In the balance sheet, assets are arranged under appropriate headings in order of permanence.
– Liabilities are items owed to others by a business.
– Liabilities are divided into two: current liabilities and longterm liabilities.
– The total of assets must equal the total of liabilities.

13.6 Revision Questions

1. Write up the balance sheet of Abegunde from the following:

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1. Write up the balance sheet of Abegunde from the following:

	N
Land and building	200,000
Plant and machinery	20,000
Stock	2,000
Debtors	4,500
Cash	50
Capital	182,000
Net profit	20,000
Long term loan	20,000
Trade creditors	4,500

2. O. Odunsi had the following balances in his books as at 31st December; 2010. Prepare his balance sheet.

Capital	45,000

	₦
Motor vehicle	57,500
Office equipments	22,500
Furniture and fittings	14,250
Net profit	5,000
Bank loan	50,000
Stock	5,000
Debtors	7,500
Creditors	7,500
Cash in hand	750

3. Balance sheet is a/an__________.

A. account

B. bank statement

C. financial statement

D. balance statements

4. Which of the following is an asset?

A. Carriage

B. Debtors

C. Creditors

D. Bank loan

5. At 31st Dec. A. Ajax had the following balances in his books:

Motor van	20,000
Premises	80,000
Capital	50,000
Cash	10,000

Debtors 15,000 Its current asset is:

A. 70,000

B. 100,000

C. 25,000

D. 95,000

6. Mr. Ajax's, fixed asset is____________.

A. 50,000

B. 130,000

C. 100,000

D. 25,000

7. In a balance sheet; assets are equal to___________.

A. cash

B. creditors

C. liabilities

D. capital