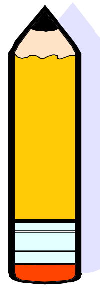
UNIT 18

ACCOUNTING



The most important goal of every accountant is to present an accurate picture of the financial health of the company. This involves *balancing the books*. Any attempt to present a false picture is called *cooking the books* or *juggling the books*. Presenting the truth means the accountant must first figure out two basic things: **what the company owns and what it owes.** If a company makes money it is *operating in the black*. If it loses money, it is *operating in the red*.

- Anything a company **owns** is called an **asset** (cash, accounts receivable, buildings, tools, equipment, etc.).
- Any money a company **owes** is called a **liability** (accounts payable, taxes, bonds, etc.)**.**

After **liabilities** are subtracted **(—)** from **assets** we may still have some money left over. This we call **owner's/shareholder's equity** or what belongs to shareholders and owners.

The most important thing to remember on a balance sheet is that....

Assets = Liabilities + Owner's equity.

In other words, what your company is worth is equal to the expenses and money left over.

The accountant's book is called a ledger. Any number entered on the left side (asset) is called **a debit**; on the right, **a credit** (liability). This necessitates the **double entry.** If you have to pay a bill (accounts payable) of $5,000 and the money comes out of cash (debit), that bill becomes a $5,000 liability (credit). Unless sales make up for it, a $5,000 liability means the owner's equity is $5,000 lower. A change on one side of the ledger necessitates a change on the other, because any figure entered on the left (asset side) must be balanced by one on the right (liability side).

Example:

Debit		***Credit***	
BEFORE	**Cash $25,000**	***Accounts payable***	***20,000***
	-5,000		***+5,000***
AFTER	**Cash $20,000**	***Accounts payable***	***$25,000***

REMEMBER: The totals on both sides must balance (be the same). That is why the accountant's report is called a **balance sheet.** (See Exercise 2)

EXERCISE 1

What is the fundamental accounting equation?

__________________ = ______________________ + __________________________

UNIT 18

EXERCISE 2
Business Terms

bond - a certificate issued by a business or government promising to pay a certain amount of interest on a specified date.
Example: You buy a 10-year $1,000 bond, but only pay $500. After 10 years, the government pays you $1,000. Since, you only paid $500 for the bond, you make $500. You may hold it and collect interest longer. When you buy a bond, you are lending money to a company or government.

long term note - a debt that must be paid over a long period of time.

patent - a legal document giving you the sole right to produce, sell or get profit from an invention or process.

deferred income tax - future taxes based on sales of goods; taxes on capital assets (machinery, equipment, property, etc.) if sold at their present value.

A) Asset or liability? Write ***A*** for asset or ***L*** for liability next to each item.

______	1)	bonds ($ 30,000)	______	8)	inventories ($ 63,000)
______	2)	cash ($ 59,400)	______	9)	deferred income tax ($ 7,587)
______	3)	accounts payable ($ 40,000)	______	10)	patents and processes
______	4)	buildings ($ 60,000)	______	11)	long term notes ($ 50,000)
______	5)	bank loans ($ 33,000)	______	12)	income taxes payable ($ 29,000)
______	6)	property ($ 25,000)	______	13)	accounts receivable ($ 11,600)
______	7)	equipment ($ 25,000)			

B) Use the information above and determine what the total **liabilities and stockholder's equity** would be. WRITE YOUR ANSWER AS ONE NUMBER.

Write your answer here: $ ____________________