THE BALANCE SHEET

Financial statements are the final product of the accounting process. The provide information on the financial condition of a company. The balance shee one type of financial statement, provides a summary of what a company own and what it owes on one particular day.

Assets represent everything of value that is owned by a business, such a property, equipment, and accounts receivable. On the other hand, liabilities ar the debts that a company owes—for example, to suppliers and banks. If liabilities are subtracted from assets (assets – liabilities), the amount remaining is th owners' share of a business. This is known as owners' or stockholders' equity.

One key to understanding the accounting transactions of a business is tc understand the relationship of its assets, liabilities, and owners' equity. This is often represented by the fundamental accounting equation: assets equal liabilities plus owners' equity.

ASSETS = LIABILITIES + OWNERS' EQUITY

These three factors are expressed in monetary terms and therefore are limited to items that can be given a monetary value. The accounting equation always remains in balance; in other words, one side must equal the other.

The balance sheet expands the accounting equation by providing more information about the assets, liabilities, and owners' equity of a company at a specific time (for example, on December 31, 1993). It is made up of two parts. The first part lists the company assets, and the second part details liabilities and owners' equity. Assets are divided into current and fixed assets. Cash, accounts receivable, and inventories are all current assets. Property, buildings, and equipment make up the fixed assets of a company. The liabilities section of the balance sheet is often divided into current liabilities (such as accounts payable and income taxes payable) and long-term liabilities (such as bonds and long-term notes).

The balance sheet provides a financial picture of a company on a particular date, and for this reason it is useful in two important areas. Internally, the balance sheet provides managers with financial information for company decision-making. Externally, it gives potential investors data for evaluating the company's financial position.

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A. Answer the following questions about the balance sheet. Questions with asterisks (*) cannot be answered directly from the text.

1. What is the final product of the accounting process?
2. What is a balance sheet?
3. Does the balance sheet provide financial information for a long period of time (for example, January to June 1993) or does it provide information for a specific point in time (for example, on June 30, 1993)?

Warm-Up

1. Look at the following two financial statements.

Thompson Electrical Products, Inc.
Balance Sheet
December 31, 1993

Assets		
Cash		$ 32,400
Accounts receivable		31,200
Inventory		38,400
Land		76,800
Building		120,000
Total assets		$ 298,800
Liabilities and Owner's Equity		
Liabilities:		
Accounts payable		$ 43,200
Mortgage payable		86,400
Total liabilities		$ 129,600
Owners' equity:		
Capital stock	$ 127,200	
Retained earnings	42,000	
Total owners' equity		$ 169,200
Total liabilities and owners' equity		$ 298,800

Thompson Electrical Products, Inc.
Income Statement
For the Month Ended Dec. 31, 1993

Revenues:		
Sales revenues		$ 110,400
Less cost of goods sold		[67,200]
Total revenues		$ 43,200
Expenses:		
Advertising	$ 2,400	
Rent	2,880	
Interest	$ 840	
Salary	$ 12,000	
Other expenses	1,560	
Total expenses		$ 19,680
Net income		$ 23,520

Figure 3

2. Review the definitions of a balance sheet and income statement on page 70. Then discuss some of the differences between the two types of financial statements with a partner. How can each type of financial statement be used in business planning?
3. Look at the balance sheet. What are its two basic categories of information?
4. Now look at the income statement. What are its three basic categories? Summarize the kind of information an income statement provides.

Preparation

1. The following list of transactions is for Canterbury Mall. Determine whether each transaction is a revenue or an expense. Mark the appropriate category of revenue or expense with an X.