



Accounting 101



ASSETS

An Asset is something that you own, that has value, and will generate a future benefit.

Assets are good.

Eg.) Cash, accounts receivable, GST receivable, inventory, equipment, land, buildings, receivable from owner, etc.



LIABILITIES

Liabilities are claims against your Assets. They are something that you have to repay to someone else.

Eg.)Accounts payable, wages payable, GST payable, long-term debt, payable to owner, etc.



EQUITY

Equity represents the owner's stake in the Assets of the company.

If the company has no Liabilities then all the Assets belong to the owner – the owner has 100% Equity in the Assets.

If the company has Liabilities then the Assets will be required to pay off those Liabilities. Whatever is left over will be the owner's Equity.

- So if the bank has claim to all of the Assets then the owner has 0% Equity.



ACCOUNTING EQUATION

Assets – Liabilities = Equity

- Eg.) Your house is worth \$500,000. You owe \$435,000 on the mortgage. Your Equity in the house is \$65,000
- You just went to Ford and bought a car for \$0 down and \$0 payments for the first 2 months. Your Equity is \$0. The finance company owns 100% of the car because you haven't paid a penny.



ACCOUNTING EQUATION

In accounting the formula is adjusted to look like:

$$\text{Assets} = \text{Liabilities} + \text{Equity}$$

In other words, all the Assets of the company can be represented by adding what the company owes to others (Liabilities) and what the owner of the company has claim to (Equity).



ACCOUNTING EQUATION

Assets are either owed (Liability) or owned (Equity) - there are no other options.

So you have Assets on the left, and Liabilities and Equity on the right. These 2 amounts always balance.

$$\text{Assets} = \text{Liabilities} + \text{Equity}$$



DEBITS AND CREDITS

Debits and Credits simply mean left and right.

DEBIT is LEFT

CREDIT is RIGHT

ASSETS = LIABILITIES + EQUITY

Debit = (Credit)

LEFT = RIGHT



DEBITS AND CREDITS

Accounting requires Debits and Credits (left and right) to ALWAYS match. The total number of Debits must equal the total number of Credits.



ASSETS AND DEBITS

Assets are Debit accounts. Debits make them bigger, Credits make them smaller.

Since Assets are a Debit account then every time we increase an Asset, we must record a matching Credit.



ASSETS AND DEBITS

1. When you sell something you either acquire cash or a receivable in return.
2. So revenue increases your Assets.
3. Assets are increased by Debits. So that means revenue must always be a Credit.

Dr. Cash \$1,000

Cr. Sales revenue \$1,000



ASSETS AND DEBITS

What if you're increasing one Asset while at the same time decreasing another Asset?

Well the Asset that's increasing is Debited and the Asset that's decreasing is Credited (remember Assets are natural Debit accounts, Debits make them bigger).

Dr. Vehicle \$70,000

Cr. Cash \$70,000



ASSETS AND CREDITS

1. When you buy something you're paying cash and decreasing your Assets.
2. So incurring expenses can decrease your Assets.
3. Assets are decreased by credits. So that means expenses must always be a debit.

Dr. Office expense	\$500	
	Cr. Cash	\$500



LIABILITIES AND CREDITS

Liabilities are the opposite of Assets. They are Credit accounts. Credits make the bigger, Debits make them smaller.

Since Liabilities are a Credit account then every time we increase an Liability, we must record a matching Debit.



Example 1

If you get a loan you increase your Assets (cash) and increase your Liability (long-term debt)

- Assets are Debit accounts, Debits make them bigger.
- Liabilities are Credit accounts, Credits make them bigger.

Dr. Cash \$500,000

Cr. Long-term debt \$500,000



Example 2

So how do you decrease a Liability?

- You have to use some Assets to pay off the loan.
- So when Liabilities are decreased Assets also decrease.
- Assets are Debit accounts, Credits make them smaller.
- Liabilities are Credit accounts, Debits make them smaller.

Dr. Accounts payable	\$1,500
Cr. Cash	\$1,500



Example 3

You're out shopping and see great sale Future Shop but you forgot you debit card at home and all you have is the company credit card. You know you shouldn't use the company's money to buy personal items but 80% off sales are just to good to let pass. You buy a new entertainment system for \$800.

How should this be recorded?



Example 3 cont'd

What are the facts?

- You purchased a items for personal use, not business use.
- The company has and \$800 credit card charge.

So in accounting terms:

- You purchased a items for personal use, not business use. **You owe the company \$800**
- The company has and \$800 credit card charge. **The company owes the credit card company \$800**



Example 3 cont'd

- The \$800 you owe is an Asset to the company. In the future the company will receive that money and be able to use it. Debits increase Assets.
- The \$800 the company has to pay Mastercard is a liability. Credits increase Liabilities.

Dr. Receivable from owner	\$800
Cr. Credit card payable	\$800



Example 4

You made a sale for \$4,000. Half was cash upfront, half is to be paid in 30 days. You use the cash you received to pay the \$100 Enmax bill and buy a \$1,700 laptop computer. How should this be recorded?



Example 4 Cont'd

What are the facts?

- The \$4,000 sale was made up of \$2,000 cash and \$2,000 to be received later.
- You spent \$1,800.

So in accounting terms:

- The \$4,000 sale was made up of \$2,000 cash and \$2,000 to be received later. **Assets are increased by \$4,000**
- You spent \$1,800. **Assets are decreased by \$1,800**
- **Assets are increased by \$1,700.**



Example 4 Cont'd

- The \$2,000 cash and \$2,000 receivable are Assets. Debits increase Assets.
- We have established earlier that revenue is a Credit. Even if you didn't know this you know that Debits have to equal Credits so the sale is a Credit by default.

Dr Cash	\$2,000	
Dr Accounts receivable	\$2,000	
Cr Sales		\$4,000



Example 4 Cont'd

- The \$1,700 laptop is an asset - you own it and it will provide future benefits. Debits increase assets.
- The \$100 Enmax bill is an expense. We know that expenses are Debits.
- You paid \$1,800 cash, that's a decrease in your Assets. Credits decrease assets.

Dr. Computer \$1,700

Dr. Utility expense \$100

Cr. Cash \$1,800



Questions ???